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TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1929

No. 114

FREDERICK C. RENZIEHAUSEN, PETITIONER,

vs.

ROBERT H. LUCAS, AS COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR CERTIORARI FILED MAY 27, 1929

CERTIORARI GRANTED OCTOBER 14, 1929

(34,245)

(34,245)

SUPREME COURT OF THE UNITED STATES

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[fol. 1]

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No., 10658

FREDERICK C. RENZIEHAUSEN, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

For Taxpayer: W. R. Seifert, Esq.
For Commissioner: J. D. Foley, Esq., A. H. Murray, Esq.

DOCKET ENTRIES

Jan.	6, 1926.	Petition received and filed.
"	12, "	Copy of petition served on Solicitor.
"	" "	**Notification of receipt mailed taxpayer.**
Mar.	12, "	Answer filed by Solicitor.
"	23, "	Copy of answer served on taxpayer—assigned to General Calendar.
Oct.	7, "	Hearing date set for 12-13-26.
Nov.	11, "	Application for order to take depositions—filed by taxpayer.
Nov.	13, "	Application for order to take depositions—filed by taxpayer.
"	22, "	Motion to change date for taking depositions filed by taxpayer.
"	23, "	Application for subpœna filed by taxpayer.
"	" "	Order to take depositions of F. L. Keelan, J. P. Hill, E. J. Siller, P. W. Gudalfinger, Robert Lewin, et al., and John M. Barton,

[fol. 2]

		signed and filed. Both sides notified.
Nov.	24, 1926.	C-oss interrogatory to be propounded to Sir James Calder—filed by G. C.
"	" "	Subpœna issued.
"	26, "	Order to take depositions, signed and filed. Both sides notified.
"	27, "	Cross interrogatory to be propounded to Patrick Hoctor, filed by G. C.
"	29, "	Order to take depositions—signed and filed. Both sides notified.

Dec. 4, 1926. Depositions of Robert Lewin filed. Copy served.
" " " Depositions of James G. Herald filed. Copy served.
" " " Depositions of A. J. Sunstein filed. Copy served.
" " " Depositions of C. W. Welty filed. Copy served.
" " " Depositions of Michael Letcelter filed. Copy served.
" " " Depositions of Jacob P. Nill filed. Copy served.
" " " Depositions of Joseph Fuhrer filed. Copy served.
" " " Depositions of John F. Gillen filed. Copy served.
" " " Depositions of D. F. Cannon filed. Copy served.
" 6, " Depositions of G. W. Schmidt filed. Copy served.
" 7, " Motion to amend embodying amendment filed by taxpayer.
" 3, " Subpœna served (R. P. Harrington),
" 11, " Application for subpœna filed by taxpayer.
" " " Subpœna issued.
" 6, " Copy of depositions served on G. C. (9)

[fol. 3]

Dec. 7, 1926. Copy of depositions served on G. C.
" 10, " Copy of motion and amended petition served on G. C.
" 16, " Depositions of Patrick Hoctor, et al., filed (1).
" 13, " Hearing had before Mr. Arundell on merits. Briefs due 2-15-27.
" 27, " Transcript of hearing Dec. 13, 1926, filed.
" 29, " Brief filed by taxpayer.
Feb. 12, 1927. Brief and findings filed by taxpayer.
" 15, " Motion for extension to 3-1-27 to file brief, filed by G. C.
" 16, " Granted—Both sides notifed.
Mar. 1, " Motion for an extension to 3-31-27 to file brief, filed by G. C.

Mar. 3, 1927. Ordered—motion be denied—and respondent allowed 15 days to file brief—signed and filed. Both sides notified.
" 12, " Brief filed by General Counsel. See 7458.
Sept. 17, " Findings of fact and opinion rendered. Order will be entered on 15 days' notice. Both sides notified.
Nov. 7, " Notice of settlement filed by G. C.
" 12, " Notice allowing taxpayer until 12-9-27 to file settlement for hearing 12-15-27, failure to do so hearing set 12-13-27.
Dec. 13, " Hearing had before Mr. Littleton on settlement, assigned to Mr. Arundell for order.
" 14, " Order of redetermination entered.
Mar. 7, 1928. Exceptions to findings of fact and conclu-
[fol. 4] sions of law lodged by taxpayer. (1)
Mar. 9, 1928. Petition for review by U. S. Cir. Ct. of Appeals 3rd Cir. with assignments of error filed by taxpayer.
" " " Proof of service filed.
May 9, " Statement of evidence lodged by taxpayer.
" " " Præcipe for transcript filed by taxpayer.
" " " Notice of service of præcipe and statement for hearing 7-15-28 with proof of service thereon, filed by taxpayer.
" 8, " Order enlarging time to August 1, 1928—entered.
" 31, " Petition for review by U. S. Cir. Ct. of Appeals 3rd Cir. with assignments of error, filed by G. C.
June 9, " Proof of service filed by G. C.
July 10, " Objections to statement of evidence filed by G. C.
" 13, " Agreed præcipe filed.
" 16, " Agreed statement of evidence approved and ordered filed.
" 13, " Order—hearing set 7-18-28 for settlement of evidence sur petition for review—entered.

Now, July 24, 1928, the foregoing Docket Entries certified from the record as a true copy.

B. D. Gamble, Clerk U. S. Board of Tax Appeals.
(Seal.)

[fol. 5] UNITED STATES BOARD OF TAX APPEALS

Docket No., 10658

Appeal of FREDERICK C. RENZIEHAUSEN, 131 Morewood Avenue, Pittsburgh, Pennsylvania

PETITION—Filed January 6, 1926

The above-named taxpayer hereby appeals from the determination of the Commissioner of Internal Revenue set forth in his deficiency letter, IT:PA:3-ATH-303-60-D, dated November 11, 1925, covering the years 1918 to 1922, inclusive, and as the basis of his appeal sets forth the following:

1. The taxpayer is an individual residing in the City of Pittsburgh, State of Pennsylvania.

2. The deficiency letter (copy of which is attached hereto) was mailed to the taxpayer on or about November 11, 1925.

3. The taxes in controversy are income taxes for the calendar years 1918 to 1922, inclusive, and are more than $10,000.00, to wit:

Year	Additional tax
1918	$186,327.72
1919	31,343.78
1920	189,887.32
1921	83,028.63
1922	69,752.49
Total	$560,339.94

[fol. 6] 4. The determination of the tax contained in the said deficiency letter is based upon the following errors:

(a) Refusal of the Commissioner of Internal Revenue to fix a value of at least $1,000,000.00, as at March 1, 1913, for the Good Will, Trade-marks, Trade-brands, etc. of The Large Distilling Company and to allow as a deduction from gross income the aliquot part of said value in the years 1918, 1919 and 1920, respectively, on account of obsolescence due to the enactment of Prohibition Laws.

(b) Refusal of the Commissioner of Internal Revenue to allow as a deduction from gross income the sum of $257,-

277.79, during the years 1918, 1919, 1920 and 1921, on account of the obsolescence of physical property, due to the enactment of Prohibition Laws, as follows:

1918 for eleven months	$61,522.95
1919 for twelve months	67,115.94
1920 for twelve months	67,115.95
1921 for eleven months	61,522.95
	$257,277.79

said physical property having a depreciated value as at January 1, 1918, of $276,652.79.

(c) Refusal of the Commissioner of Internal Revenue to fix a value of at least $1,257,277.79 for the properties of The Large Distilling Company, exclusive of land and to allow as a deduction from gross income the sum of $1,257,-277.79 during the years 1918, 1919, 1920 and 1921, on account of the obsolescence of properties, due to the enactment of Prohibition Laws.

(d) Refusal of the Commissioner of Internal Revenue to tax as capital gain, under Section 206 of the Revenue Act of [fol. 7] 1921, at the rate of 12½%, the gain realized in the year 1922 from the sale of "Old Whiskey," a personal investment of Frederick C. Renziehausen made at least five years prior to date of sale.

(e) Refusal of the Commissioner of Internal Revenue to fix a value of at least $250,000.00, as at March 1, 1913, for the Good Will of Schuetz, Renziehausen & Company, a partnership, of which the taxpayer was a member; and to allow said partnership, as a deduction from gross income, the aliquot part of said value in the years 1918, 1919 and 1920, respectively, on account of obsolescence, due to the enactment of Prohibition Laws.

5. The facts upon which the taxpayer relies as the basis of his appeal are as follows:

(a) The taxpayer owned and operated a distillery located at Large, Pennsylvania, under the name, The Large Distilling Company, a sole proprietorship.

This distillery was first operated by Jonathan Large in the year 1796, who was succeeded by his son, and in 1862

by his grandson, Henry Large, Jr., who continued to operate the business until 1884.

At that time, Messrs. Frederick C. Renziehausen and Thomas Delaney came into the firm and the name, The Large Distilling Company, was adopted. In 1889, Thomas Delaney retired and his brother, James Delaney, became associated with the business. James Delaney retired in 1891.

After the death of Henry Large, Jr., in 1895, the business was continued by his widow and Frederick C. Renziehausen.

In 1897, Mrs. Anna H. Large retired and Frederick C. Renziehausen became sole owner of the business. The firm had been operated as a partnership under the name, The Large Distilling Company, up to this time, and Mr. Renziehausen continued to use this name after he became the sole [fol. 8] owner of the business. The business was registered in this name in the State of Pennsylvania.

This business was 122 years old when the Eighteenth Amendment was passed in January, 1918, and had built up a large and valuable "Good Will," including Trade-marks, Trade-brands, etc., in the beverage whiskey trade during this period.

The product of this distillery was "Large" pure rye whiskey only, which was sold in bond on contract prior to its manufacture to select distributors. Contractors settled for and took title to the new whiskey in bond, on negotiable warehouse receipts, during the production season, and assumed all carrying charges.

The quality of this brand of whiskey was acknowledged by first prizes awarded at the following international expositions:

Chicago,	in	the	year	1893,
Paris	"	"	"	1900,
St. Louis,	"	"	"	1904,
Liege,	"	"	"	1905,
Milan,	"	"	"	1906,
Jamestown	"	"	"	1907,
Brussels,	"	"	"	1910,
Ghent,	"	"	"	1913,

and San Francisco in the year 1915.

The taxpayer has, since his sole ownership of this trade-

mark and up to the enactment of prohibition, invested over $220,000 in publicity of this brand, as follows:

Invested in publicity from date of sole ownership to March 1, 1913	$138,281.12
From March 1, 1913, to date of prohibition	82,509.47
Total	$220,790.59

[fol. 9] The tangible assets as of June 30, 1908, to 1912, inclusive, were as follows:

June 30, 1908	$362,205.20
June 30, 1909	351,873.80
June 30, 1910	437,984.45
June 30, 1911	527,498.27
June 30, 1912	607,203.66
Total	$2,286,765.38
Average	$457,353.07

The net income for the years 1909 to 1913, inclusive, was as follows:

1909	$88,815.70
1910	89,513.82
1911	79,705.39
1912	85,003.03
1913	112,517.94
Total	$455,555.88
Average	$91,111.18

A fair return on tangible assets as at March 1, 1913, was 5 per cent. Money was available at banks and brokerage houses at that time at 3 per cent.

The distilling business was very staple and not subject to fluctuation, as was the case in other commercial activities.

The method followed by the Commissioner in valuing intangibles; that is, by allowing a certain return on the tangibles and capitalizing the balance at another rate, does not reflect the true value of the intangibles of The Large Distilling Company. The value of The Large Distilling Company's goodwill, trade-marks, trade brands, etc., on March 1, 1913, was in excess of $1,000,000.

[fol. 10] (b) Congress in January, 1918, passed the Eighteenth Amendment and at this time the taxpayer determined, and it became an established fact, that within a period of approximately four years his distillery would be obsolete.

In November, 1921, the President of the United States signed the Willis-Campbell Act, which prohibited the distillation of whiskey for medicinal purposes without a permit from the Commissioner of Internal Revenue. The said Commissioner has refused to issue any permits whatsoever since that time, and no whiskey has been legally distilled in the United States since that date.

The date on which obsolescence first took effect was January 31, 1918, and the end of the obsolescence period was November 23, 1921.

The depreciated value of the physical assets on December 31, 1917, was $276,652.79. The salvage value was $19,375, leaving a balance of $257,277.79 which the taxpayer is entitled to deduct from gross income as obsolescence, spread over the period January 31, 1918, to November 31, 1921, as follows:

Year	Period	Amount
1918	11 months	$61,522.95
1919	12 "	67,115.94
1920	12 "	67,115.95
1921	11 "	61,522.95
	46 months	$257,277.79

(c) The taxpayer owned and operated a distillery located at Large, Pennsylvania, under the name, The Large Distilling Company, a sole proprietorship.

This distillery was first operated by Jonathan Large in the year 1796, who was succeeded by his son, and in 1862 by his grandson, Henry Large, Jr., who continued to operate the business until 1884.

[fol. 11] At that time, Messrs. Frederick C. Renziehausen and Thomas Delaney came into the firm and the name, The Large Distilling Company, was adopted. In 1889 Thomas Delaney retired and his brother, James Delaney, became associated with the business. James Delaney retired in 1891.

After the death of Henry Large, Jr., in 1895, the business was continued by his widow and Frederick C. Renziehausen.

In 1897 Mrs. Anna H. Large retired and Frederick C. Renziehausen became sole owner of the business. The firm had been operated as a partnership under the name, The Large Distilling Company, up to this time, and Mr. Renziehausen continued to use this name after he became the sole owner of the business. The business was registered in this name in the State of Pennsylvania.

This business was 122 years old when the Eighteenth Amendment was passed in January, 1918, and had built up a large and valuable "goodwill," including trade-marks, trade brands, etc., in the beverage whiskey trade during this period.

The product of this distillery was "Large" pure rye whiskey only, which was sold in bond on contract prior to its manufacture to select distributors. Contractors settled for and took title to the new whiskey in bond, on negotiable warehouse receipts, during the production season, and assumed all carrying charges.

The quality of this brand of whiskey was acknowledged by first prizes awarded at the following international expositions:

Chicago, in the year 1893.
Paris, in the year 1900.
St. Louis, in the year 1904.
Liege, in the year 1905.
Milan, in the year 1906.
[fol. 12] Jamestown, in the year 1907.
Brussels, in the year 1910.
Ghent, in the year 1913,
and San Francisco in the year 1915.

The taxpayer has, since his sole ownership of this trademark and up to the enactment of prohibition, invested over $220,000 in publicity of this brand, as follows:

Invested in publicity from date of sole ownership to March 1, 1913	$138,281.12
From March 1, 1913, to date of prohibition	82,509.47
Total	$220,790.59

The tangible assets as of June 30, 1908, to 1912, inclusive, were as follows:

June 30, 1908	$362,205.20
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Total	$2,286,765.38
Average	$457,353.07

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1909	$88,815.70
1910	89,513.82
1911	79,705.39
1912	85,003.03
1913	112,517.94
Total	$455,555.88
Average	$91,111.18

[fol. 13] A fair return on tangible assets as at March 1, 1913, was 5 per cent. Money was available at banks and brokerage houses at that time at 3 per cent.

The distilling business was very staple and not subject to fluctuation, as was the case in other commercial activities.

The method followed by the Commissioner in valuing intangibles; that is, by allowing a certain return on the tangibles and capitalizing the balance at another rate, does not reflect the true value of the intangibles of The Large Distilling Company. The value of The Large Distilling Company's goodwill, trade-marks, trade brands, etc., on March 1, 1913, was in excess of $1,000,000.

Congress, in January, 1918, passed the Eighteenth Amendment and at this time the taxpayer determined, and it became an established fact, that within a period of approximately four years his distillery would be obsolete.

In November, 1921, the President of the United States signed the Willis-Campbell Act, which prohibited the distillation of whiskey for medicinal purposes without a permit from the Commissioner of Internal Revenue. The said

Commissioner has refused to issue any permits whatsoever since that time, and no whiskey has been legally distilled in the United States since that date.

The date on which obsolescence first took effect was January 31, 1918, and the end of the obsolescence period was November 23, 1921.

The depreciated value of the physical assets on December 31, 1917, was $276,652.79. The salvage value was $19,375, leaving a balance of $257,277.79 which the taxpayer is entitled to deduct from gross income as obsolescence, spread over the period January 31, 1918, to November 31, [fol. 14] 1921, as follows:

Year	Period	Amount
1918	11 months	$61,522.95
1919	12 "	67,115.94
1920	12 "	67,115.95
1921	11 "	61,522.95
	46 months	$257,277.79

(d) In the year 1908, the taxpayer had (among other personal investment accounts) an additional private investment account opened up and carried as a matter of convenience on the books of The Large Distilling Company under the caption "Old Whiskey a/c."

This account represented a personal investment of Mr. Frederick C. Renziehausen in Large whiskey distilled by The Large Distilling Company, and it is not part of and at no time has it been included in the inventory or stock in trade of the company.

The inventory and stock in trade of the Large Distilling Company consisted of grain, cooperage, fuel, bottling supplies and other materials used at the distillery and warehouse receipts for a small quantity of bonded whiskey in Mdse P & S a/c. The "Merchandise, Purchase and Sales" account was opened on the books of The Large Distilling Company, and all purchases and sales of bonded whiskey were made through this account. This account was handled by The Large Distilling Company.

In 1922 all the whiskey in "Old Whiskey a/c" had been carried therein five years or more, and had been "interned" in bond since July 1, 1919.

The total profit from the sale of "Old Whiskey" accruing to Mr. Frederick C. Renziehausen personally, in the year 1922, amounted to $134,922.36, which amount is made up as follows:

[fol. 15] Barrels	Gallons	Date acquired	Date sold	Amount received	Cost	Net gain
7.....	323.34	6/30/16	2/ 2/22	$1,107.89	$151.96	$955.93
41.....	1,921.50	6/30/16	2/21/22	6,580.80	903.10	5,677.70
50.....	2,350.67	6/30/16	2/21/22	8,050.35	1,104.81	6,945.54
40.....	1,883.95	6/30/16	4/ 6/22	6,450.82	885.46	5,565.36
45.....	2,079.41	6/30/16	4/ 6/22	7,116.59	977.32	6,139.27
100.....	4,635.85	6/30/16	5/ 3/22	15,860.48	2,178.85	13,681.63
75.....	3,454.75	6/30/16	5/24/22	11,814.13	1,623.73	10,190.40
100.....	4,588.46	6/30/16	6/ 6/22	15,689.61	2,156.58	13,533.03
29.....	1,340.12	6/30/16	8/23/22	4,578.77	629.86	3,948.91
60.....	2,753.69	6/30/17	10/ 6/22	8,050.82	1,842.22	6,208.60
100.....	4,589.84	6/30/17	10/16/22	13,415.02	3,070.60	10,344.42
200.....	9,202.16	6/30/17	10/31/22	26,892.73	6,156.25	20,736.48
300.....	13,754.65	6/30/17	10/15/22	40,196.95	9,201.86	30,995.09
Total Capital Gain.....						$134,922.36

(e) The partnership, Schuetz, Renziehausen and Company, was formed in 1879, and consisted of three partners until 1892, when one of the partners died. Since that time the business has been conducted by Frederick C. Renziehausen and Henry Schuetz, Jr.

The partnership was formed for the purpose of buying and selling liquors, etc. to wholesale and retail trade. Since organization it has built up a large and valuable goodwill.

This business was 39 years old when the Eighteenth Amendment was enacted by Congress.

Mr. Henry Schuetz, Jr. and Mr. Frederick C. Renziehausen, the taxpayer, owned and operated this partnership, 50 per cent of the profits being credited to each partner at the end of each year, and 50 per cent of any operating loss being absorbed by each partner.

The tangible assets of this partnership, as at the beginning of the years 1908 to 1912, inclusive, were as follows:

[fol. 16]	1908	$277,398.99
	1909	293,376.47
	1910	310,365.54
	1911	329,537.80
	1912	337,738.49
	Total	$1,548,417.29
	Average	$309,683.46

The net income of this partnership for the years 1908 to 1912, inclusive, was as follows:

1908	$27,755.00
1909	31,442.81
1910	34,889.38
1911	22,421.78
1912	22,387.75
Total	$138,896.72
Average	$27,779.34

The value of the goodwill and other intangibles at March 1, 1913, of the partnership, Schuetz, Renziehausen and Company, was $250,000.00, all of which was destroyed by the enactment of the National Prohibition Act. The obsolescence of said goodwill took place from January 31, 1918, to January 16, 1920, and should be spread, as a deduction from gross income, over said years as follows:

1918	$117,021.19
1919	127,659.48
1920	5,319.33
Total	$250,000.00

In the years 1918, 1919 and 1920, the income of the taxpayer should be reduced as follows:

[fol. 17] 1918	$58,510.60
1919	63,829.74
1920	2,659.66

6. The taxpayer, in support of his appeal, relies upon the following propositions of law, covering his respective claims under (a), (b), (c), (d) and (e).

(a) In computing the net income of a taxpayer, there shall be allowed as a deduction for the obsolescence of goodwill, etc., valued as at March 1, 1913.

(b) In computing the net income of a taxpayer, there shall be allowed a deduction for the obsolescence of physical property.

(c) In computing the net income of a taxpayer there shall be allowed a deduction for the obsolescence of properties exclusive of land.

(d) In computing the taxes due from an individual taxpayer after December 31, 1921, there shall be allowed, if he so elects, a rate of 12½ per cent. on all capital net gain.

(e) In computing the net income of a taxpayer, there shall be allowed a deduction for the obsolescence of goodwill valued as at March 1, 1913.

Wherefore the taxpayer respectfully prays that this Board may hear and determine his appeal.

W. A. Seifert, Counsel. W. A. Seifert, Counsel, 747 Union Trust Building, Pittsburgh, Pennsylvania,

[fol. 18] *Duly sworn to by F. C. Renziehausen. Jurat omitted in printing.*

[fol. 19] Letter, Dated Nov. 11, 1925

Form NP-2

(U. S. T. Dept. Seal.)
Office of Commissioner of Internal Revenue.
Address Reply to Commissioner of Internal Revenue and Refer to IT:PA:3. ATH-303-60 D.

Treasury Department, Washington

Nov. 11, 1925.

Mr. Frederick C. Renziehausen, 131 Morewood Avenue, Pittsburgh, Pennsylvania.

SIR: The determination of your income tax liability for the taxable years 1918 to 1922, inclusive, as set forth in office letter dated January 7, 1925, disclosed an aggregate deficiency in tax amounting to $560,339.94.

In accordance with the provisions of Section 274 of the Revenue Act of 1924, you are allowed 60 days from the date of mailing of this letter within which to file an appeal to the United States Board of Tax Appeals contesting in whole or in part the correctness of this determination.

Where a taxpayer has been given an opportunity to appeal to the United States Board of Tax Appeals and has not done so within the 60 days prescribed and an assessment has been made, or where a taxpayer has appealed and an assessment in accordance with the final decision on such appeal has been made, no claim in abatement in respect of any part of the deficiency will be entertained.

If you acquiesce in this determination and do not desire to file an appeal, you are requested to sign the inclosed agreement consenting to the assessment of the deficiency and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:PA:3-ATH-303-[fol. 20] 60D. In the event that you acquiesce in a part of the determination, the agreement should be executed with respect to the items agreed to.

Respectfully, D. H. Blair, Commissioner, by C. R. Nash, Assistant to the Commissioner.

Inclosures: Statements, Agreement—Form A, Form 882.

Statement

IT:PA:3. ATH-303-60 D.

In re Mr. Frederick C. Renziehausen, 131 Morewood Avenue, Pittsburgh, Pennsylvania

Year	Deficiency in tax
1918	$186,327.72
1919	31,343.78
1920	189,887.32
1921	83,028.63
1922	69,752.49
Total	$560,339.94

The audit of your returns for the years 1918 to 1922, inclusive, and of your books of account and records as disclosed in office letter to you dated January 7, 1925, has been sustained.

[fol. 21] In regard to the value of good will of the Large Distilling Company, since you continued to manufacture and sell whiskey under Government permit after the Prohibition Amendment went into effect, it is held that you are

not entitled to obsolescence of good will unless on the effective date of the Prohibition Amendment or prior thereto you discontinue the business and do not engage in a similar business.

The above reasons also apply to the partnership business of Schuetz Renziehausen and Company with relation to the obsolescence of good will and of plant and equipment, since it has not been shown when the plant was definitely abandoned.

In regard to the application of the capital gain provisions under Section 206 of the Revenue Act of 1921, it has been held that the account shown as the "Old whiskey account" was actually a part of the general inventory and as such was properly handled in the audit.

Relative to the obsolescence of the three-story brick building used for storage purposes, it is noted by the supplemental report that the building is still used for storing purposes and, therefore, is not abandoned at this date, nor has there been submitted any conclusive evidence to show when the building will be abandoned.

This assessment is in addition to all other outstanding and unpaid assessments appearing upon the Collector's list.

Payment of the deficiency in tax should not be made until a bill is received from the Collector of Internal Revenue for your district, and remittance should then be made to him. [fol. 22] Now, July 24, 1928, the foregoing petition certified from the record as a true copy.

B. D. Gamble, Clerk U. S. Board of Tax Appeals.
(Seal.)

Before United States Board of Tax Appeals

Docket No., 10658

In re Appeal of Frederick C. Renziehausen, Pittsburgh, Pennsylvania

Answer—Filed March 12, 1928

The Commissioner of Internal Revenue, by A. W. Gregg, Solicitor of Internal Revenue, his attorney, for answer to the petition heretofore filed by the above-named taxpayer, admits and denies as follows:

(1) Admits the allegations of paragraphs numbered 1, 2 and 3.

(2) Admits that the taxpayer was the sole owner and operator of the distillery located at Large, Pennsylvania, and known as the Large Distilling Company.

(3) Denies that the value of the good will of the distilling business of the taxpayer was on March 1, 1913, $1,000,000 or any amount whatsoever.

(4) Denies that at any time prior to the adoption of the Eighteenth Amendment or at any time thereafter taxpayer determined that within a period of approximately four years or within any period his distillery would be obsolete.

[fol. 23] (5) Denies that the depreciated value of the physical assets of the distillery was on December 31, 1917, $276,552.79, or any amount.

(6) Denies that in the year 1908 the taxpayer had a private investment account and carried as a matter of convenience on the books of the Large Distilling Company (which was himself) under the caption of "Old Whiskey Account."

(7) Denies that old whiskey represented by this account was not part of the stock in trade of the taxpayer's business.

(8) Admits that the partnership Schuetz, Renziehausen & Company was formed in 1879 and that it consisted of three partners until 1892, when one of the partners died and that since that time the business has been conducted by Frederick C. Renziehausen and Henry Schuetz, Jr.

(9) Denies that the value of the good will and other intangibles of this partnership was on March 1, 1913, $250,000 or any amount.

(10) Denies generally and specifically each and every allegation not hereinbefore admitted, qualified or denied.

Propositions of Law

(1) The taxpayer is not entitled to obsolescence on either tangibles or intangibles due to the adoption of the Eighteenth Amendment.

(2) Part of the taxpayer's stock in trade is not a capital asset within the meaning of Section 206 of the Revenue Act of 1921.

[fol. 24] Wherefore it is prayed that said petition be denied.

A. W. Gregg, Solicitor of Internal Revenue, Attorney for Commissioner of Internal Revenue. Of Counsel: John D. Foley, Special Attorney, Bureau of Internal Revenue.

Now, July 24, 1928, the foregoing answer certified from the record as a true copy.

B. D. Gamble, Clerk U. S. Board of Tax Appeals. (Seal.)

Before United States Board of Tax Appeals

Docket No., 10658

In re Mr. Frederick C. Renziehausen, 131 Morewood Avenue, Pittsburgh, Pennsylvania

Motion to Amend Petition—Filed December 7, 1926

Comes now the petitioner, by his counsel, W. A. Seifert, and moves to amend the petition heretofore filed by filing the annexed amendments.

W. A. Seifert, Counsel for Taxpayer.

Dated December 6, 1926.

[fol. 25] Before United States Board of Tax Appeals

Docket No., 10658

Appeal of Frederick C. Renziehausen, 131 Morewood Avenue, Pittsburgh, Pennsylvania

Amendments to Petition—Filed December 7, 1928

The petition is hereby amended by adding to paragraph 4 thereof subparagraph (f), as follows:

(f) Erroneous inclusion by the Commissioner of Internal Revenue of the sum of $31,015.50 in taxable income for 1920 as profit on the sale of whiskey, whereas in fact such profit was not realized.

The petition is hereby further amended by striking out the last paragraph on page 13 thereof and the schedule at the top of page 14 thereof, both being a part of subparagraph (d) of paragraph 5, and substituting the following therefor:

(d) The total profit from the sale of "Old Whiskey" accruing to Mr. Frederick C. Renziehausen personally in the year 1922 amounted to $196,545.24, which amount is made up as follows:

Original cost	Bottling, tax, and other costs	Total cost	Selling price	Total gain
$33,928.26	$117,237.42	$151,165.68	$347,710.92	$196,545.24

The petition is hereby further amended by adding to paragraph 5 subparagraph (f), as follows:

(f) During the year 1920 and in other years, subsequent thereto, the taxpayer kept the books of his business, known as The Large Distilling Company, upon a departmental [fol. 26] basis. The whiskey owned by the taxpayer was carried in various accounts on the books of The Large Distilling Company at cost. During the year 1920 such whiskey was bottled prior to its sale as medicinal whiskey and tax was paid thereon as required by law. The whiskey was taken over on the books of the Large Distilling Company at a figure in excess of the figure at which it was carried in the various accounts in which it previously appeared, and the difference was considered and entered upon the books as a profit. After the whiskey was so taken over it was bottled by the taxpayer, who was doing business under the name of The Large Distilling Company, and after being bottled was transferred to the medicinal whiskey account on the books of The Large Distilling Company and at that time another profit was taken on those books as a profit on bottling. Finally, the whiskey was sold, and at that point another profit was entered on the books of The Large Distilling Company, being the difference between selling price

of the whiskey and the sum of the following: Cost at which the whiskey was originally carried and cost of bottling and bottling profit, together with other expense. As a matter of fact, the first two of the three profits in this paragraph mentioned were not profits at all, but mere book entries, for the reason that Frederick C. Renziehausen and The Large Distilling Company were one and the same individual and no profit was or could be realized until the whiskey was actually sold to some other person. Taxable profit on the sale of such whiskey accrued when the whiskey was sold and was equal to the difference between selling price and total cost to the taxpayer, including tax, cost of bottling, and all other expenses. On his return for the year 1920 the [fols. 27 & 28] taxpayer, through error, included the sum of $31,015.50 as profit on the sale of whiskey, but said sum was not profit, either realized or otherwise, but consisted of mere book entries as in this paragraph described, and the whiskey on which such book profit was taken was not actually sold until subsequent to the close of the year. The field agent made corrections and adjustment for like items for the years 1923, 1924 and 1925, but no such correction has been made for the years 1920, 1921 and 1922.

W. A. Seifert, Counsel for Taxpayer.

Duly sworn to by F. C. Renziehausen. Jurat omitted in printing.

Certificate to foregoing paper omitted in printing.

[fol. 28-1] Before U. S. Board of Tax Appeals

Request for Findings of Fact and Conclusions of Law—Filed Feb. 12, 1927

And now, February —, 1927, comes the Petitioner, by his attorney, W. A. Seifert, and respectfully requests this Honorable Board to make the following findings of fact and conclusions of law in the above entitled case:

Request for Findings of Fact

1. Petitioner is an individual, residing in the City of Pittsburgh, Pennsylvania.

Answer. ——.

2. Petitioner, during the years 1918 to 1922, both inclusive, was the sole proprietor of The Large Distilling Company.

Answer. ——.

3. The Petitioner, during the years 1918 to 1920, was a partner in the firm of Schuetz, Renziehausen & Company, of Pittsburgh, Pennsylvania.

Answer. ——.

4. The plant of The Large Distilling Company was located in Jefferson Township, Allegheny County, Pennsylvania.

Answer. ——.

[fol. 28-2] 5. The business which was carried on by The Large Distilling Company until November, 1921, was established in 1796. The firm of Schuetz, Renziehausen & Company consisted of Henry Schuetz, Jr., and the Petitioner, and was founded in 1879.

Answer. ——.

6. The Large Distilling Company's business was that of distilling or manufacturing rye whiskey.

Answer. ——.

7. The business of the firm of Schuetz, Renziehausen & Company, until the effective date of prohibition, was that of selling whiskeys, wines, brandies, cordials, etc., at wholesale.

Answer. ——.

8. As of March 1, 1913, the Large Distilling Company owned trade marks, trade brands, trade names, etc., as follows: Five-pointed star within a star; the label "Large Whiskey"; the slogan "Drink a Little Large"; the Company also had registered the label "Large, Established 1796, Monongahela Pure Rye Whiskey"; "Pure Monongahela Rye Whiskey Made by Henry Large, Jr., Pittsburgh, Pennsylvania" within a circle.

Answer. ——.

[fol. 28-3] 9. The trade mark for the star within a star was acquired from the estate of Henry Large on July 19th, 1897, at a cost of $5,000.00.

Answer. ——.

10. Large Whiskey was distributed by wholesale and retail dealers throughout the whole of the United States. It was bottled in bond under Government supervision.

Answer. ——.

11. The Large Distilling Company exhibited its product at ten international expositions, viz: Chicago, 1893; Paris, 1900; St. Louis, 1904; Liege, 1905; Milan, 1906; Jamestown, 1907; Brussels, 1910; Ghent, 1913; London, 1914 and San Francisco, 1915; at which the Company was awarded the grand prizes at nine expositions, which were the highest possible awards. Eight of these international expositions were before March 1, 1913.

Answer. ——.

12. Prior to March 1, 1913, the company did extensive advertising in trade journals, theater programs, price lists and at local expositions. Its advertising, which included paying for excess leakage, was done at a cost of $138,281.12, all of which was expended prior to March 1, 1913.

Answer. ——.

[fol. 28-4] 13. The distilling business was a stable business. It required a great many years to build it up and get the confidence of the public to which its product was sold. As much as two or three generations were required to build up such a business.

Answer. ——.

14. For the past 22 years the petitioner in operating The Large Distilling Company used his own capital and did not have to borrow any money from any bank. Over the same period, he did not discount any of his customers' notes. He was not a speculator in whiskeys.

Answer. ——.

15. The distilling business, as carried on by the Petitioner, consisted of the manufacture of whiskey for wholesale liquor dealers under contract. Substantially all the whiskey made by The Large Distilling Company was sold to wholesalers on contract before it was made.

Answer. ——.

16. Prior to and subsequent to March 1, 1913, The Large Distilling Company's business was rapidly expanding. The reputation of Large Whiskey in the trade and its standing with consumers was the very highest. The selling price per gallon of Large Whiskey in bond was always [fol. 28-5] higher than that of any other rye whiskey.

Answer. ——.

17. Over the period from June 30, 1908 to June 30, 1912, the value of The Large Distilling Company's tangible assets

averaged $251,380.05. The earnings from his distilling business for the years ending June 30, 1909, 1910, 1911, 1912 and 1913 averaged $91,111.18.

Answer. ——.

18. On March 1, 1913, 5 per cent was a fair return on the tangible property invested in The Large Distilling Company and 10 per cent was a fair return on the intangibles in that business.

Answer. ——.

19. The March 1, 1913, value of the trade marks, trade brands, trade names, goodwill, etc., of The Large Distilling Company was at least $1,000,000.00.

Answer. ——.

20. The firm of Schuetz, Renziehausen & Company had a very substantial business and catered to an exclusive trade.

Answer. ——.

[fol. 28-6] 21. Schuetz, Reinziehausen & Company owned registered trade marks for "Fort Pitt Whiskey," "Diamond Monogram Whiskey" and "Crusader Dry Gin," all of which were acquired prior to March 1, 1913.

Answer. ——.

22. The tangible assets of the partnership for the years 1908 to 1912, inclusive, averaged approximately $309,000.00 and the average income of the partnership for the same period was approximately $27,000.00.

Answer. ——.

23. The value of the trade marks, trade brands, trade names, goodwill, etc., of the firm of Schuetz, Renziehausen & Company, on March 1, 1913, capitalized on the basis of 5 per cent and 10 per cent was $115,500.00.

Answer. ——.

24. By January 31, 1918, it was certain that the Constitutional Amendment would be ratified. It became effective the 16th day of January, 1920. The Willis-Campbell Act was approved November 23, 1921. The Large Distilling Company made whiskey until November 21, 1921, for medical purposes, when further manufacture was stopped on ac-
[fol. 28-7] count of the Willis-Campbell Act. No whiskey was manufactured after that date.

Answer. ——.

25. Petitioner, in 1918, determined that in about four years the manufacture of whiskey would be brought to an

end by effective legislation and that the distilling business would have to be wound up.

Answer. ——.

26. The value of the trade marks, trade brands, trade names, goodwill, etc., of The Large Distilling Company, as of March 1, 1913, was entirely wiped out by the Constitutional Amendment and the passage of the Willis-Campbell Act.

Answer. ——.

27. The Large Distilling Company has been in the process of liquidation since the last whiskey was manufactured in the Fall of 1921.

Answer. ——.

28. Petitioner has liquidated his "Old Whiskey" as fast as was possible in accordance with the rules and regulations of the Prohibition Department, to authorized permitees.

Answer. ——.

[fol. 28-8] 29. The obsolescence of the March 1, 1913, value of the trade marks, trade brands, trade names, goodwill, etc., of The Large Distilling Company occurred over the period January 31, 1918 to November 30, 1921, inclusive.

Answer. ——.

30. On January 16, 1920, the firm of Schuetz, Renziehausen & Company started liquidating its goods.

Answer. ——.

31. After January 16, 1920, the stock of the firm of Schuetz, Renziehausen & Company which was not liquidated was disposed of as fast as was possible. A permit was obtained to liquidate to the wholesale and retail drug trade. It was not possible to liquidate the fine liquors and wines on permits to the wholesale and retail drug trade. A permit was obtained to donate the remaining stock to hospitals in accordance with their authorized quota. This took too long to dispose of the remaining floor stock and it was dumped into the sewers of the building, under Government supervision.

Answer. ——.

32. The obsolescence of the March 1, 1913 value of the trade marks, trade brands, trade names, goodwill, etc., of the firm of Schuetz, Renziehausen & Company occurred

[fol. 28-9] over the period January 31, 1918, to January 16, 1920.

Answer. ——.

33. Prior to March 1, 1913, the Large Distilling Company paid out the sum of $138,281.12 for advertising purposes, all of which was properly the cost of developing the goodwill.

Answer. ——.

34. For a period of twenty-nine years prior to March 1, 1913, the Petitioner contributed his services to The Large Distilling Company without receiving any compensation therefor. These services had a total value of $435,000.00, all of which was properly the cost of developing the goodwill of the Company.

Answer. ——.

35. The cost of developing the goodwill was properly made up of the following items:

Advertising	$138,281.12
Cost of services	435,000.00
Cash paid July 19, 1897	5,000.00
Total	$578,281.12

Answer. ——.

[fol. 28-10] 36. No whiskey was manufactured in the United States after the passage of the Willis-Campbell Act and of course none was manufactured by The Large Distilling Company. The Large Distilling Company has been in liquidation since November 21, 1921. In 1918, the Petitioner determined that it would be about four years before the distillation of whiskey would be entirely prohibited. He knew at that time that within approximately that period the distilling business would have to be wound up.

Answer. ——.

37. The depreciated value of The Large Distilling Company's physical property on December 31, 1917, was $276,652.79. The salvage value on November 30, 1921, was $19,375.00. The physical property of The Large Distilling Company which became obsolete over the period January 31, 1918, to November 30, 1921, had a value of $257,277.79.

Answer. ——.

38. The obsolescence of the physical properties of The Large Distilling Company having the value of $257,277.79 should be spread as follows:

1918 for eleven months	$61,522.95
1919 for twelve months	67,115.94
1920 for twelve months	67,115.95
1921 for eleven months	61,522.95
Total	$257,277.79

Answer. ——.

[fol. 28-11] 39. The business of The Large Distilling Company has been in liquidation since November 21, 1921. All of the whiskey sold by Petitioner on which profit was realized in the year 1922 was held for more than two years. The whiskey which was sold in 1922 was sold from what is known as the "Old Whiskey" account. This was a personal investment made by the Petitioner in whiskey representing the production at the end of the distilling season, which had not been sold or delivered on contracts. When sold in 1922 it had been carried for more than four or five years.

Answer. ——.

40. The "Old Whiskey" was not stock in trade or other property which would properly be included in the inventory of the Petitioner, but it was property held by the Petitioner for profit and investment.

Answer. ——.

41. "Old Whiskey" was not a part of The Large Distilling Company's inventory or stock in trade. The trade of The Large Distilling Company had been wiped out by the enactment of the Constitutional Amendment. The Petitioner started to liquidate the business of The Large Distilling Company on November 21, 1921. The manufacture of whiskey ceased in the United States on November 21, 1921. The business ceased to exist. The Petitioner had no alternative. He was not in a position to carry on a like business. He was forced to liquidate.

Answer. ——.

[fol. 28-12] 42. The net income for the year 1922, before making deduction for depreciation, is $185,393.55. This income after adjustment for depreciation is subject to tax at the capital gain rate of 12½ per cent.

Answer. ——.

43. The taxable income for the year 1920 was overstated in the sum of $31,015.50, on account of an inter-account profit. It should be reduced by that amount.

Answer. ——.

44. The taxable income for the year 1921 was understated in the sum of $1,637.14. Due to an error in failing to take up realized inter-account profit, the income for the year 1921 should be increased by that amount.

Answer. ——.

45. The taxable income for the year 1922 was understated in the sum of $5,248.44. Due to an error in failing to take up realized inter-account profit, the income for the year 1922 should be increased by that amount. The error in the sum of $5,248.44 for the year 1922 is reflected in the increased income for that year, as shown in Petitioner's Exhibit 37 and Commissioner's Exhibit "B."

Answer. ——.

[fol. 28-13] Request for Conclusions of Law

1. The Petitioner is entitled, under Sections 214 (a) (8) of the Revenue Acts of 1918 and 1921, to deductions from gross income for the years 1918, 1919, 1920 and 1921 for obsolescence of the March 1, 1913, value of trade marks, trade brands, trade names, goodwill, etc., of The Large Distilling Company.

Answer. ——.

2. The Petitioner is entitled, under Section 214 (a) (8) of the Revenue Act of 1918, to deductions from gross income for the years 1918, 1919 and 1920 for obsolescence of the March 1, 1913, value of trade marks, trade brands, trade names, goodwill, etc., of the firm of Schuetz, Renziehausen & Company.

Answer. ——.

3. The Petitioner is entitled, under Sections 214 (a) (8) of the Revenue Acts of 1918 and 1921, to deductions from gross income for the years 1918, 1919, 1920 and 1921 for obsolescence of plant and equipment of The Large Distilling Company.

Answer. ——.

[fol. 29] 4. The Petitioner is entitled, under Section 206 of the Revenue Act of 1921, to have The Large Distilling

Company's net income for the year 1922 taxed at the rate of 12½ per cent.

Answer. ——.

If Points 1, 2 and 3 should not be affirmed, it is respectfully requested that this Board make the following conclusions of law:

1. The Petitioner is entitled, under Section 214 (a) (8) of the Revenue Act of 1918, to a deduction from gross income for the year 1919 of the cost of the trade marks, trade brands, trade names, goodwill, etc., of The Large Distilling Company destroyed by the ratification of the Eighteenth Amendment on January 16, 1919.

Answer. ——.

2. The Petitioner is entitled, under Section 214 (a) (8) of the Revenue Act of 1921, to a deduction from gross income for the year 1921 for the loss of the useful value of the plant and equipment of The Large Distilling Company.

Answer. ——.

[fol. 30] 3. The Petitioner is entitled, under Sections 214 (a) (8) of the Revenue Acts of 1918 and 1921, respectively, to deductions from gross income for the years 1918, 1919, 1920, 1921 and 1922 for depreciation sustained.

Answer. ——.

Respectfully submitted.

W. A. Seifert, Smith, Shaw & McClay, Attorneys for Petitioner.

[fol. 31] Before United States Board of Tax Appeals

Docket Nos., 10658 and 7458

Frederick C. Renziehausen, Petitioner,

v.

Commissioner of Internal Revenue, Respondent

Henry Schuetz, Jr., Petitioner,

v.

Commissioner of Internal Revenue, Respondent

Findings of Fact, Opinion and Decision—Filed September 17, 1927

Deduction for obsolescence of intangibles denied upon authority of Red Wing Malting Company v. Levi M. Will-

cuts, 15 Fed. (2d) 626, and Appeal of Manhattan Brewing Company, 6 B. T. A. 952.

Petitioner discontinued the manufacture of intoxicating liquors in 1917 under the restrictions of war-time prohibition. In 1919 it resumed distilling operations for the manufacture of medicinal whiskey and continued to distill whiskey for medicinal purposes until forced to discontinue on November 23, 1921, by the enactment of the Willis-Campbell Act. In 1922, the last year on appeal, petitioner was still disposing of its stock in trade, under the same trademarks, trade name, and trade brands as it used prior to prohibition, but under different methods and to a different clientele. Held, that petitioner's intangibles were not de- [fol. 32] stroyed on January 16, 1919, when ratification of the Eighteenth Amendment was completed; and that it suffered no deductible loss in any of the years on appeal, by virtue of destruction of intangibles by prohibition legislation.

Upon the evidence, held, that petitioner is not entitled to deductions for 1918, 1919 and 1920 for obsolescence of tangible properties.

Petitioner's entire distilling plant, other than its bonded warehouses, was rendered obsolete by the passage of the Willis-Campbell Act on November 23, 1921, and the continued refusal of the Commissioner of Internal Revenue to issue permits for the manufacture of medicinal whiskey under the provisions of that Act; and petitioner is entitled to a deduction for 1921 for obsoleteness of its plant facilities, the amount of which is herein determined.

Upon the evidence, held, that certain whiskey sold by petitioner in 1922 was property of a kind which would properly have been included in his inventory, had it been on hand at the close of that year, and that the profit from the sale of such whiskey is taxable as ordinary income under Section 201 of the Revenue Act of 1921, and not as a capital gain under Section 206.

W. A. Seifert, Esq., for the Petitioners.
John D. Foley, Esq., for the Respondent.

These proceedings were consolidated for hearing and decision. In the case of Frederick C. Renziehausen, respondent has determined deficiencies of $186,327.72 for

1918, $31,343.78 for 1919, $189,887.32 for 1920, $83,028.63 for 1921, and $69,752.49 for 1922. In the case of Henry Schuetz, Jr., respondent has determined deficiencies of $13,652.11 for 1918, $277.20 for 1920, and $637.98 for 1921, [fol. 33] and an overassessment of $670.67 for 1919.

In the case of Frederick C. Renziehausen the issues are: (1) Respondent's refusal to allow deductions from income of the years 1918, 1919, and 1920 for obsolescence of godwill, trade-marks, trade names, and trade brands of the Large Distilling Company, having an alleged value of $1,000,000 at March 1, 1913; (2) respondent's refusal to allow a loss deduction for 1919 for obsoleteness of the goodwill, trade-marks, trade names, and trade brands of the Large Distilling Company; (3) respondent's refusal to allow deductions from income of 1918, 1919, 1920, and 1921, for obsolescence of the tangible properties of the Large Distilling Company, having a book value and alleged depreciated value of $276,652.79 at January 1, 1918; (4) respondent's refusal to allow a loss deduction for 1921 for obsoleteness of the tangible properties of the Large Distilling Company; (5) respondent's refusal to allow deductions from income of the years 1918, 1919, 1920, and 1921, for obsolescence of the tangible and intangible properties of the Large Distilling Company; (6) respondent's refusal to allow deductions for obsolescence of goodwill in computing the income of the partnership of Schuetz, Renziehausen & Company for the years 1918, 1919, and 1920; (7) failure of respondent to allow any deductions for depreciation of the physical assets of the Large Distilling Company, in computing income for 1918, 1919, 1920, and 1921; (8) respondent erred in including in income of 1920 an alleged profit of $31,015.50 from the sale of certain whiskey; and (9) respondent's refusal to tax as a capital gain, under Section 206 of the Revenue Act of 1921, the profit from the sale of certain whiskey, in 1922.

In the case of Henry Schuetz, Jr., there are but two issues: (1) Respondent's refusal to allow deductions for obsolescence of goodwill in computing the income of the [fol. 34] partnership of Schuetz, Renziehausen & Company for 1918, 1919, and 1920; and (2) respondent erred in determining that petitioner realized a profit of $260.25 from the sale of certain real property in 1920.

Findings of Fact

Frederick C. Renziehausen is a resident of Pittsburgh, Pennsylvania, and sole owner of the whiskey distilling business conducted under the trade name of the Large Distilling Company. He was also the owner of a one-half interest in the partnership of Schuetz, Renziehausen & Company, wholesale liquor dealers, in Pittsburgh.

Henry Schuetz, Jr., is a resident of Pittsburgh, Pennsylvania, and, during the years on appeal owned a one-half interest in the partnership of Schuetz, Renziehausen & Company.

In 1796 Jonathan Large founded a whiskey distilling business, under the trade name of the Large Distilling Company, at Mount Washington (now a part of Pittsburgh), Pennsylvania. Three years later the distillery was moved to Jefferson Township, Allegheny County, Pennsylvania, where the business has been carried on since that time. From 1884 to 1897 the business was conducted as a partnership, composed of Henry Large and his wife, and the petitioner, Renziehausen. In 1897 Renziehausen became sole owner of the business, and thereafter to the present time conducted it as a sole proprietorship.

The business of the Large Distilling Company was principally that of distilling whiskey, which it sold to wholesale liquor dealers under uniform contracts. It also carried on a warehousing business, storing the whiskey which it distilled in its bonded warehouses until matured and withdrawn by the owners, for which the latter paid the monthly [fol. 35] storage charges stipulated in the sales contracts. It also bottled and cased the matured whiskey in bond, for which it received compensation from the owners thereof. From time to time, with varied frequence, it purchased warehouse receipts for whiskey in its own bonded warehouses and resold the same at a profit. It carried the whiskey left over from each distilling season to various stages of maturity, and, as opportunities were afforded, disposed of it to the trade.

During September and October of each year a close watch was kept on growing grain crops and the trend of the Chicago and Milwaukee grain markets, to observe the prevailing prices for grain. Based upon these observations, the

price for the whiskey to be distilled in the following winter and spring was fixed, and contracts were then solicited from the wholesale trade based upon that price. The contracts were printed and uniform, and for the distilling season of 1916-1917 read, in terms and figures, as follows:

"Established 1796

The Large Distilling Company

P. O. Box 1050, Pittsburgh, Pa.

Distillers of Large Rye Whiskey

Large, Penn'a, —— —, 191-.

To —— ——:

We propose to distill for your account (—) — barrels Large Rye Whiskey, to be delivered in our U. S. Bonded Warehouse, on our distillery premises, located at Large, on Peters Creek, Allegheny County, Pennsylvania, (contingent upon strikes and unavoidable accidents) as follows:

— Bbls. in November, 1916.
— Bbls. in December, 1916.
— Bbls. in January, 1917.
— Bbls. in February, 1917.
— Bbls. in March, 1917.
— Bbls. in April, 1917.
— Bbls. in May, 1917.
— Bbls. in June, 1917.

[fol. 36] At 65 cents per proof gallon, Net Cash, original gauge, in bond. Rate of storage, five (5) cents per bbl. per month.

Respectfully submitted.

The Large Distilling Company.

Accepted —— —, 191-. —— ——, per —— ——.

The whiskey required to fill the contracts was distilled in the following fall and spring; placed in Government bonded warehouses, and the warehouse certificates therefor turned over to the owners of the whiskey according to the quantities purchased. After the whiskey had remained

in the warehouses for the time required by Government regulations, usually four years, it was bottled in bond, under Government supervision, by the Large Distilling Company for the owners of the whiskey.

"Large" whiskey, by which name the product of the Large Distilling Company was generally known, was distributed by wholesale and retail liquor dealers throughout the whole of the United States. It was generally regarded by the wholesole trade as one of the leading rye whiskeys of the country. For a long period prior to 1913 and thereafter until the Large Distilling Company ceased distilling for beverage purposes in 1917, there was a steady growth in the demand for "Large" whiskey. The company seldom operated its distillery to full capacity. It was the practice to determine upon the quantity of whiskey to be distilled in the following season before soliciting contracts from the wholesale trade, and contracts were accepted with due regard to the total quantity to be distilled. Usually the quantity specified in the contract of a particular wholesale dealer was based upon the quantity upon which that dealer was making tax payments. The purpose of this was to [fol. 37] prevent as far as practicable, speculation in warehouse receipts for "Large" whiskey. Because of these business practices, the demand for "Large" whiskey, as a general rule, exceeded the supply.

From 1899 to 1913, inclusive, the Large Distilling Company expended for advertising the total sum of $82,500.02; and from 1914 to 1921, inclusive, it expended for the same purpose the total sum of $86,155.61. The advertising consisted of installing exhibits at local and international expositions, well-designed show cards, and displays in leading trade journals, newspapers, theatre programs, whiskey blotters, and the distribution of price lists. It exhibited its product at ten international expositions, viz: Chicago, 1893; Paris, 1900; St. Louis, 1904; Liege, 1905; Milan, 1906; Jamestown, 1907; Brussels, 1910; Ghent, 1913; London, 1914; and San Francisco, 1915; at nine of which it was awarded the grand prizes.

In addition to the amounts expended specifically for advertising, the Large Distilling Company, between 1899 and 1913, inclusive, paid to its customers the total sum of $55,-

781.10 for leakage; and from 1914 to 1921, inclusive, it expended for the same purpose the following amounts:

1914	$2,048.20
1915	2,228.97
1916	3,187.33
1917	1,297.23
1918	948.61
1919	368.28
1920	1,753.74
1921	1,467.78
Total	$13,300.14

Leakage refers to the evaporation while the whiskey is stored in the Government bonded warehouses in excess of [fol. 38] the Government allowance, and upon which the owners of the whiskey were required to pay the tax. The tax on excess evaporation was paid by the owners and they were reimbursed by the Large Distilling Company, although there was no specific provision in the contracts under which the company could be held liable.

On July 19, 1897, the Large Distilling Company purchased a trade-mark for $5,000 cash.

At March 1, 1913, the Large Distilling Company owned trade-marks, trade-names and trade brands as follows: Five-pointed star within a star; the label "Large Whiskey;" the slogan "Drink a Little Large;" and the company also had registered the label "Large, Established 1796, Monongahela Pure Rye Whiskey;" and "Pure Monongahela Rye Whiskey Made by Henry Large, Jr., Pittsburgh, Pennsylvania" within a circle.

For the years 1908 to 1912, inclusive, the books of account of the Large Distilling Company show tangible property employed in the business and earnings, as follows:

Year	Tangible property	Earnings
1908	$141,412.94	$88,815.70
1909	231,824.43	89,513.82
1910	240,337.04	79,705.39
1911	292,226.98	85,003.03
1912	351,099.53	112,517.94
Total	$1,256,900.92	$455,555.88
Average	251,380.18	91,111.18

From the time he became a partner in the Large Distilling Company in 1884 to and including 1912 the petitioner Renziehausen was not paid any salary for his personal services. A reasonable compensation for the period 1908 to 1912, inclusive, for the services he rendered to the business would have been $15,000 per annum.

[fol. 39] In December, 1907, shortly after distilling operations for the season of 1907-1908 had commenced, the Large Distilling Company's distillery was destroyed by fire. The distillery was rebuilt shortly thereafter, but no more whiskey was distilled until the following distilling season. Had not the fire occurred the company during the succeeding four or five years, would have received income from the storing and bottling of the whiskey which would have been distilled in the season of 1907-1908.

During the past 22 years the petitioner Renziehausen has carried on the business of the Large Distilling Company entirely with his own funds; no borrowed money has been employed in the business during that time.

The business of the Large Distilling Company, or any interest or any share therein, has never been offerred for sale during the time ownership has vested in the petitioner Renziehausen.

The last whiskey produced by the Large Distilling Company for beverage purposes, was distilled in May, 1917. Thereafter and until January 16, 1920, the effective date of the Eighteenth Amendment, no whiskey could be produced for beverage purposes because of war-time prohibition. With the imposition of war-time prohibition and the progress which had been made toward adoption of the Eighteenth Amendment, Renziehausen became convinced in 1918 that the distilling part of the business of the Large Distilling Company was through for all time, and that the business as a whole would be entirely wound up and liquidated within four years. During 1919 Renziehausen became aware that he could lawfully manufacture whiskey for medicinal purposes; and in the fall of that year the Large Distilling Company resumed distilling operations for the production of whiskey for medicinal purposes and continued such operations until at or about November 23, 1921, [fol. 40] when, because of the enactment of the so-called Willis-Campbell Act which provided that whiskey could be manufactured for medicinal purposes only under permits

issued by the Commissioner of Internal Revenue, and petitioner having failed to secure such a permit, distilling operations ceased. No whiskey has been manufactured by the Large Distilling Company since November 23, 1921. No permits for the production of medicinal whiskey have been issued, under the provisions of the Willis-Campbell Act, by the Commissioner of Internal Revenue.

The Large Distilling Company manufactured whiskey for medicinal purposes in 1919, 1920 and 1921 in the followings quantities:

1919	396	barrels
1920	5,858	"
1921	10,400	"
Total	16,654	"

The cost of the physical properties of the Large Distilling Company, exclusive of land, at January 1, 1918, the accrued depreciation at the same date, and the depreciation sustained in 1918, 1919, 1920, and 1921, are as follows:

Item	Cost to January 1, 1918	Accrued depreciation January 1, 1918
Railroad siding	$2,498.63	$1,207.64
Buildings (new)	151,413.53	14,636.63
Bonded warehouses	115,413.53	10,989.97
Machinery & Equipment	97,035.72	48,517.84
Unused equipment (new)	2,657.13	1,284.24
Buildings (old)	5,833.85	1,399.83
Delivery equipment	182.77	176.65
Unused equipment (old)	1,329.75	1,285.42
Boiler House & stack	16,316.33	155.66
Totals	$329,681.24	$79,653.88

[fol. 41]

Item	Depreciation sustained in 1918	1919	1920	1921
Railroad siding	$249.86	$249.86	$249.86	$229.04
Buildings (new)	3,028.27	3,028.27	3,028.27	2,765.91
Bonded warehouses	2,308.27	2,308.27	2,308.27	2,308.27
Machinery & Equipment	9,703.57	9,703.57	9,703.57	8,894.94
Unused equipment (new)	265.71	265.71	265.71	243.57
Buildings (old)	291.69	291.69	291.69	267.38
Delivery equipment	6.12	.....	.....	.....
Unused equipment (old)	44.33	.....	.....	.....
Boiler House & Stack	326.33	326.33	326.33	299.15
Totals	$16,224.15	$16,173.70	$16,173.70	$15,008.26

Of the physical properties above listed, none, other than the bonded warehouses, have been put to any use since cessation of distilling operations on or about November 23, 1921. None of them are adaptable to any other purpose than the processes of manufacturing whiskey. The salvage value of the physical properties, not including that of the bonded warehouses, is $19,375.

The four bonded warehouses are of the rack type of construction for the storage of whiskey in barrels, and they are not adaptable to any other purpose. Their total capacity is 55,000 barrels. Their salvage value, because of the type of construction, location, and cost of demolition, is nil. All four of the warehouses were being used for the storage of whiskey during the years on appeal and as late as 1923, and the extent to which they were being used is indicated by the following:

Year	Number of barrels in storage Jan. 1	Number of barrels stored during year	Number of barrels withdrawn during year
1918	35,365	None	11,183
1919	24,182	396	6,478
1920	18,100	5,858	5,234
1921	18,724	10,400	1,731
1922	27,393	None	1,761
1923	25,632	....	....

[fol. 42] Prior to January 1, 1918, the Large Distilling Company disposed of the whiskey it manufactured, in bulk, exclusively to the wholesale liquor trade. Such sales of whiskey manufactured after that date as have been made have been to persons holding Government permits to purchase whiskey for medicinal purposes, and have consisted entirely of bottled in bond whiskey.

The business of the Large Distilling Company has been in process of liquidation since the fall of 1921.

In his deficiency determination respondent refused to allow a deduction for any of the years on appeal for obsolescence or for obsoleteness of the tangible or intangible properties of the Large Distilling Company.

The firm of Schuetz, Renziehausen & Company was founded in 1879 by the petitioners Renziehausen and Schuetz and Frederick Guedemann. Guedemann died in

1892 and the business was carried on thereafter, until liquidated in 1925, by the petitioners, Renziehausen and Schuetz, as equal partners. The business of the partnership was that of wholesale liquor dealers, selling brandies, cordials, fine liquors, and wines. At March 1, 1913, and thereafter until January 16, 1920, the effective date of the Eighteenth Amendment, the firm enjoyed the patronage of the most substantial retailers in the territory in which it did business.

At March 1, 1913, Schuetz, Renziehausen & Company owned registered trade-marks for "Fort Pitt Whiskey," "Diamond Monogram Whiskey," and "Crusador Dry Gin."

For the years 1908 to 1912, inclusive, the books of account show tangible property employed in the business and earnings, as follows:

Year	Tangible property	Earnings
[fol. 43] 1908	$277,398.99	$27,755.00
1909	293,376.47	31,442.81
1910	310,365.54	34,889.38
1911	329,537.80	22,421.78
1912	337,738.49	22,387.75
Totals	$1,548,417.29	$138,896.72
Average	$309,683.46	$27,779.34

Liquidation of the business of Schuetz, Renziehausen & Company was begun in 1920 and completed in 1925. When prohibition legislation became effective its stock of merchandise consisted of brandies, cordials, gins, other fine liquors, and wines. The wholesale and retail drug trade would not buy this class of merchandise. A permit was obtained from the Commissioner of Internal Revenue to donate the stock to hospitals in accordance with their authorized quota, but this method of liquidation took too long and in 1925 all of the remaining stock was dumped in the sewers of the building, under Government supervision.

In his deficiency determinations in the cases of both petitioners respondent refused to allow deductions from the income of the partnership of Schuetz, Renziehausen & Company for the years 1918, 1919 and 1920 for obsolescence of intangibles.

In his deficiency determination in the case of the petitioner Renziehausen respondent failed to allow any deduc-

tion for any of the years on appeal for depreciation of the physical properties of the Large Distilling — deduction for any of the years on appeal for depreciation, exclusive of any allowance for obsolescence, are as follows:

1918	$16,224.15
1919	16,173.70
1920	16,173.70
1921	15,008.26

[fol. 44] The net income shown in the deficiency notice for 1920 is overstated by $31,015.50 by virtue of respondent erroneously including an alleged profit of that amount upon an alleged sale of whiskey in that year; and the net income shown in the deficiency notice for 1921 and 1922 is understated by $1,637.14 and $5,248.44, respectively, by virtue of respondent's failure to include certain profits earned in those years.

In 1908 there was opened on the books of the Large Distilling Company an account captioned "Old Whiskey." At the close of each distilling season the whiskey manufactured and not sold was charged to this account and carried to maturity when it was sold to the trade through the organization of the Large Distilling Company. In 1922 all of the whiskey then carried in this account was sold and at the date of the sale it had been held for profit for more than two years. Renziehausen regarded the whiskey carried in this account as a personal investment. Over a long period of time the petitioner Renziehausen had carried personal investments on the books of the Large Distilling Company. Respondent in the deficiency determination refused to tax the profit from the sale of this whiskey as a capital gain at the rate of 12½ per cent. under the provisions of section 206 of the Revenue Act of 1921.

Opinion

ARUNDELL:

In the case of Henry Schuetz, Junior, respondent determined an overassessment for 1919; hence, the Board is without jurisdiction of the issue raised for that year. Appeal of R. P. Hazzard Company, 4 B. T. A. 150; and Appeal of Cornelius Cotton Mills, 4 B. T. A. 255.

The first issue in Renziehausen's appeal is that respondent erred in refusing to allow deductions from the income

[fol. 45] of 1918, 1919 and 1920 for obsolescence of intangibles of the Large Distilling Company, of which he was sole proprietor, resulting from prohibition legislation, based upon an alleged March 1, 1913, value for such intangibles of $1,000,000. The issue has already been decided adversely to the petitioner by the Circuit Court of Appeals, Eighth Circuit, in Red Wing Malting Company v. Levi M. Willcuts, Collector, 15 Fed. (2nd) 626, and by this Board in Appeal of Manhattan Brewing Company, 6 B. T. A. 952; and on this issue we must find for respondent.

The second issue, which is alternative to the first, is that respondent erred in refusing to allow a deduction for 1919 for obsoleteness of the intangibles of the Large Distilling Company, resulting from prohibition legislation, based upon an alleged cost of $578,281.12. Petitioner contends that if the Board holds against him on the first issue then it must find that the intangibles of the Large Distilling Company were wholly destroyed on January 16, 1919, when ratification of the Eighteenth Amendment was completed by the required number of States, and that he is entitled to a loss deduction for that year measured by the cost of the intangibles, which cost he computes as follows:

For services rendered by petitioner without compensation 1884 to 1913 (29 years at $15,000 per annum)	$435,000.00
Advertising, 1899 to 1913	82,500.02
Leakage, 1899 to 1913	55,781.10
Trade-mark acquired for cash, July 19, 1897	5,000.00
Total cost of intangibles	$578,281.12

The facts preclude such finding. The mere ratification of the Eighteenth Amendment did not destroy the business of [fol. 46] the Large Distilling Company or render its intangibles obsolete, for it continued to carry on the business after January 16, 1919, and after the Eighteenth Amendment and enforcement legislation became effective in 1920, under the same trade-marks, trade name, and trade brand although modified somewhat as to methods by reason of such legislation. Prior to 1919 the Large Distilling Company sold its product before it was manufactured to the wholesale liquor trade and made delivery in bulk in an unmatured state at its bonded warehouses. Beginning with

1919 its whiskey was matured in bonded warehouses, bottled in bond, and disposed of to the wholesale and retail drug trade or others holding Government permits. As late as 1922, the last year we have for review, the Large Distilling Company was still disposing of its whiskey stock under the same trade-marks, trade name, and trade brands, and there is no record evidence as to when, if at all, the business was finally terminated. Prohibition wrought changes in the method of doing business and in the character of its clientele, but the business which it carried on both before and after prohibition became effective, and throughout all of the years under review, was essentially the same. We see no proper grounds upon which to base a deduction for 1919 or any other year on appeal for obsoleteness of intangibles of the Large Distilling Company.

The third issue in Renziehausen's appeal is that respondent erred in refusing to allow deductions from the income of 1918, 1919, 1920 and 1921 for obsolescence of the tangible property of the Large Distilling Company. Petitioner contends that with the imposition of war-time prohibition and the progress made in 1918 toward final adoption of the Eighteenth Amendment it became apparent in that year that the business of the Large Distilling Company would have to be wound up within four years, and that the de- [fol. 47] preciated value of the tangible assets at January 1, 1918, less salvage value, should be obsolesced over the period February 1, 1918, to November 30, 1921. The petitioner Renziehausen testified at the hearing that because of the progress of national prohibition in 1918 he became convinced in that year that "the jig was up"; that the distilling part of the business was through for all time and the business as a whole would have to be wound up in about four years; and that he did not discover until some time in 1919 that the Large Distilling Company could continue distilling whiskey for medicinal purposes. The Large Distilling Company resumed distilling operations in 1919 and continued such operations until forced to discontinue in November, 1921, by virtue of the enactment of the Willis-Campbell Act and failure to secure a permit to continue distilling operations as provided in that Act.

Obsolescence, we have held, is the state or process of becoming obsolete, and the state of obsoleteness is reached when the property which cannot be used for any other pur-

pose is no longer useful for the purpose for which it was acquired. Appeal of Columbia Malting Company, 1 B. T. A. 999; Appeal of Manhattan Brewing Company, 6 B. T. A. 952. The right to an obsolescence deduction must be based upon substantial reasons for believing that assets would become obsolete prior to the end of their ordinary useful life; and it must have been known, or believed to have been known, to a reasonable degree of certainty, under all the facts and circumstances, when that event would likely occur. Appeal of Columbia Malting Company, supra; Appeal of Cleveland Home Brewing Company, 1 B. T. A. 87. Under the circumstances of this case it cannot be held that the tangible assets of the Large Distilling Company were in a state or condition of becoming obsolete in 1918, 1919, or 1920. Renziehausen thought he was through in 1918, but his convictions were based upon a lack [fol. 48] of knowledge of his lawful rights; and in 1919 he resumed distilling operations and continued to carry on such operations until the enactment of the Willis-Campbell Act on or about November 23, 1921. The plant facilities of the Large Distilling Company were being used at the close of 1919 and 1920 for the purposes for which they had been acquired, and apparently without any diminution as to usage prior to prohibition legislation. It was the passage of the Willis-Campbell Act in 1921 which prohibited the manufacture of medicinal whiskey except under permits issued by the Commissioner of Internal Revenue, and the continued refusal of that officer to issue such permits, which forced the petitioner to discontinue distilling operations and rendered the plant facilities of the Large Distilling Company, other than its bonded warehouses, obsolete; and this event could not have been foreseen in 1918, 1919 or 1920. As Renziehausen testified, the passage of the Willis-Campbell Act came suddenly, like a bolt out of a clear sky, and he did not at the time consider the passage of that Act possible. We find no error in respondent's refusal to allow deductions from the income of 1918, 1919 and 1920, for obsolescence of the tangible properties of the Large Distilling Company. As to 1921, we think obsoleteness of the tangible properties, other than the bonded warehouses, took place wholly within that year, by virtue of the enactment of the Willis-Campbell Act and the

continued refusal of the Commissioner of Internal Revenue to issue permits, under that Act, for the manufacture of medicinal whiskey. As to the amount of the deduction for that year, we leave that for determination under the next issue.

The fourth issue in Renziehausen's appeal, which is alternative to the third, is that the respondent erred in refusing to allow a deduction for 1921 for obsoleteness of the tangi- [fol. 49] ble properties of the Large Distilling Company. We think that the tangible properties of the Large Distilling Company, other than its bonded warehouses, were rendered entirely obsolete in 1921 by virtue of the enactment of the Willis-Campbell Act, which prohibited the manufacture of medicinal whiskey except under permits issued by the Commissioner of Internal Revenue, and the continued refusal of that officer to issue such permits. We have set out in the findings of fact the cost of these properties, the depreciation sustained thereon, and the salvage value thereof, and upon the basis of those facts we find that the petitioner is entitled to a loss deduction, for 1921, for obsoleteness of the tangible properties of the Large Distilling Company, exclusive of the loss on bonded warehouses, of $147,582.06.

As to the four bonded warehouses, we are of the opinion that petitioner suffered no deductib-e loss in 1921 in respect thereof. Unlike the other plant facilities which had become obsolete and were abandoned, the warehouses were continued in use for the purpose for which they had been constructed. It is true that these facilities were being used at only 50 per cent of their maximum capacity, and existing conditions at the close of 1921 indicate no greater usage in the future; but the very fact that the facilities were in use is sufficient proof that they had not reached the end of their useful life. Obsoleteness connotes lack of usefulness and absence of value; and where facilities are being used, whether at maximum or a lesser capacity, neither of those factors are present. The extent to which facilities are being used is of no importance whatever, for if they are being put to any use at all the very opposite of a state of obsoleteness is indicated.

However, it is apparent that the passage of the Willis-Campbell Act, on November 23, 1921, and the continued

refusal of the Commissioner of Internal Revenue to issue permits for the manufacture of medicinal whiskey, pre-
[fol. 50] cluded the possibility of any further use for these warehouses than for the storage of the whiskey on hand on November 23, 1921. For this reason, we are of the opinion that the passage of the Willis-Campbell Act marked the beginning of the obsolescence of these warehouses. When the whiskey stored in these warehouses has been finally withdrawn, the latter will have no useful purpose in petitioner's business, and because of type of construction they cannot be adapted or converted to any other purpose than the storage of whiskey in bulk. This latter fact, coupled with those of location and cost of demolition, indicate that at the close of the obsolescence period the value of these warehouses will be nil. It is impracticable to measure the obsolescence period in terms of years, since it is impossible to foretell the length of time which will pass before the whiskey will be withdrawn. A measure, then, to determine the annual deduction for obsolescence, other than that of effluxion of time, must be applied here.

The warehouses in question had a total capacity of 55,-000 barrels; and, while there is no evidence in the record bearing directly on this point, we are inclined to believe, from such facts as we have, that this capacity did not exceed the normal needs of the business. The evidence shows that no whiskey was manufactured between May, 1917, and December 31 of that year, because of the restrictions imposed, by the "Food Control" acts, upon the use and transportation of cereals and grains for beverage purposes; and that on January 1, 1918, there were 35,365 barrels of whiskey stored in these warehouses. Had it not been for the restriction imposed by the "Food Control" acts, petitioner could have continued to manufacture whiskey during 1917, and the quantity of whiskey on hand, at January 1, 1918, would have been greater by at least the normal pro-
[fol. 51] duction of the fall and winter distilling season of 1917. Considering these circumstances in conjunction with what is common knowledge—that reserve facilities are indispensable in a growing manufacturing business—we are led to the conclusion that the total capacity of the warehouses was needed in petitioner's business.

The situation confronting this petitioner, then on November 23, 1921, when the Willis-Campbell Act was passed, was precisely one in which the useful and valuable capacity of the four bonded warehouses was reduced from 55,000 to 27,393 barrels, with definite indications that no greater capacity could be used, or would be needed, in the future, and that as the whiskey, then on hand, was withdrawn the useful and valuable capacity would be correspondingly diminished.

The deduction for obsolescence, we believe, like those for depreciation and depletion, should be based upon actualities, as nearly as that may be possible; and this is necessary if the deductions is to be a "reasonable" one as the statute contemplates. To require that the entire obsolescence should be spread and deducted from income as the remaining 27,393 barrels of whiskey, at the close of 1921, are withdrawn, would result in postponing the entire obsolescence deduction to years subsequent to 1921, when as a matter of fact obsolescence was sustained in that year to the extent of the reduction in the useful and valuable capacity of the warehouses. In view of the foregoing, it is our opinion that the petitioner is entitled to a deduction, for 1921, for obsolescence of the warehouses, in an amount representing the same proportion of the depreciated cost as the number of barrels representing the reduction in the useful and valuable capacity, plus the number of barrels withdrawn from November 24, to December 31, 1921, to wit: 27,607, bears to 55,000; and that for 1922 petitioner is entitled to a like deduction based upon the proportion which [fol. 52] the number of barrels withdrawn during that year, to wit: 1,761, bears to 55,000 or in such manner that when the entire amount of whiskey has been withdrawn the entire cost of the buildings shall be returned by way of obsolescence and depreciation.

The fifth issue in Renziehausen's appeal, which is alternative to the four preceding it, is that respondent erred in refusing to permit deductions from the income for 1918, 1919, 1920 and 1921, for obsolescence of the tangible and intangible properties of the Large Distilling Company; and for reasons given in our consideration of the first four issues, we held the respondent committed error only in respect of his denial of a deduction, for 1921, for obsolescence of the four bonded warehouses.

The sixth issue in Renziehausen's appeal and the first issue of Henry Shuetz, Junior, is that respondent erred in refusing to permit deductions for obsolescence of good will in computing the income of the partnership of Shuetz, Renziehausen & Company for 1918, 1919, and 1920. The issue has already been decided adversely to the petitioners in Red Wing Malting Company v. Levi F. Willcuts, Collector, 15 Fed. (2d) 626, and in Appeal of Manhattan Brewing Company, 6 B. T. A. 952, and upon authority of these cases we find respondent's action in denying the claimed deductions is proper.

At the hearing the parties placed in evidence a joint exhibit showing the cost of the physical properties of the Large Distilling Company at January 1, 1918, and the depreciation sustained in 1918, 1919, 1920, and 1921; and the respondent conceded error in failing to allow deductions for depreciation in those years. The deduction to which the petitioner Renziehausen is entitled for depreciation of the physical assets of the Large Distilling Company is $16,224.15 for 1918 and $16,173.70 for each of the years 1919 and 1920. For 1921 the petitioner is entitled to a de- [fol. 53] duction for depreciation, including obsolescence of the bonded warehouses, in the amount of $50,088.70, and to no further deduction for depreciation of the other physical assets enumerated in the findings of fact, because the deduction allowed for that year, in this opinion, for obsoleteness, is inclusive of depreciation. For 1922 Renziehausen is entitled to a deduction for depreciation, including obsolescence, of the bonded warehouses, in the amount of $2,827.33. This disposes of the seventh issue in Renziehausen's appeal.

The eighth issue in Renziehausen's appeal is that respondent erred in including in income for 1920 an alleged profit of $31,015.50 from the sale of certain whiskey. At the hearing respondent conceded error as to this issue; and the parties stipulated that as a result of this adjustment the net income shown in the deficiency notice for 1921 and 1922 should be increased $1,637.14 and $5,248.44, respectively.

The ninth issue in Renziehausen's appeal is that respondent erred in refusing to tax the profit from the sale of certain whiskey in 1922 as a capital gain at 12½ per cent., as

provided in Section 206 of the Revenue Act of 1921. The whiskey in question was that which had been carried on the books of the Large Distilling Company in the account captioned "Old Whiskey." Petitioner contends that this whiskey was not a part of stock in trade, but his own investment, which had been held for profit for more than two years at the date of the sale; and that the profit derived from the sale thereof in 1922 is a capital gain, subject to tax at 12½ per cent.

Section 206 of the Revenue Act of 1921, so far as material here, reads as follows:

"That for the purpose of this title:

"(1) The term 'capital gain' means taxable gain from the sale or exchange of capital assets consummated after December 31, 1921;

* * * * * * *

[fol. 54] "(6) The term 'Capital assets' as used in this section means property acquired and held by the taxpayer for profit or investment for more than two years (whether or not connected with his trade or business), but does not include property held for personal use or consumption of the taxpayer or his family, or stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year."

Renziehausen, for he and the Large Distilling Company are the same person, was engaged in the business of distilling and selling whiskey, and as incidents to the conduct of such business, he bought and sold the product of his own plant whenever warehouse receipts were available for purchase, and he matured the excess of each season's production and sold it to the trade. The petitioner was engaged in more than a distilling business; he was also trading in whiskey. Whiskey was his stock in trade. Beginning in 1908, the excess production of each distilling season was charged on the books of the Large Distilling Company to the "Old Whiskey" account. As this whiskey matured, or perhaps in some cases prior to complete maturity, the whiskey was sold by, and through the organization of, the Large Distilling Company. It is not in evidence whether

the profits from the sale of this whiskey, as sales were made in prior years, were included in the earnings of the Large Distilling Company, or withdrawn by the petitioner, or credited to his account. The whiskey sold in 1922 was a part of the whiskey carried in this account and represented the accumulation of excess production of several distilling seasons. It was property of a kind which would properly have been included in the petitioner's inventory, had it been on hand at the close of the year 1922, and, therefore, does not come within the statutory definition of capital assets.

[fol. 55] Petitioner makes the alternative contention that all of the income of the Large Distilling Company for 1922 should be treated as capital gain, since the business was being liquidated from November, 1921, and the inventory became a frozen capital asset when liquidation began. But neither does this contention appear to us to be tenable. Whatever stock in trade the Large Distilling Company had on hand when liquidation commenced continued to be inventoriable stock in trade until disposed of. Its character was not in the least changed because of the fact that the business was in process of liquidation. We find no error in respondent's action in refusing to treat the profit derived from the sale of old whiskey in 1922 as a capital gain.

The second issue in the appeal of Henry Schuetz, Junior, is that respondent erred in determining a profit of $260.25 from the sale of certain real property in 1290. No evidence was adduced in support of this allegation of error and the issue is not touched upon in the brief filed by the petitioner after the hearing. The issue has been abandoned, apparently, by the petitioner.

Reviewed by the Board.

In the Appeal of Frederick C. Renziehausen, Docket No. 10658, order of redetermination will be entered on 15 days' notice, in accordance with Rule 50. In the Appeal of Henry Schuetz, Junior, Docket No. 7458, judgment will be entered for respondent as to the years 1918, 1920, 1921, and an order of dismissal as to the year 1919.

Now, July 24, 1928, the foregoing findings of fact and opinion certified from the record as a true copy.

B. D. Gamble, Clerk U. S. Board of Tax Appeals.
(Seal.)

[fol. 56] BEFORE UNITED STATES BOARD OF TAX APPEALS, WASHINGTON

Docket No., 10658

FREDERICK C. RENZIEHAUSEN, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

ORDER OF REDETERMINATION—Filed December 14, 1927

Pursuant to the decision of the board heretofore rendered in the above-entitled proceeding, the respondent having filed a proposed redetermination and notice of settlement, and no objection to said proposed redetermination and notice of settlement having been made by the petitioner, after due notice thereof, it is

Ordered and Decided that there are deficiencies for the years 1918, 1919, 1920 and 1922 in the respective amounts of $174,159.60, $22,495,44, $156,362.99 and an overassessment for the year 1921 in the amount of $23,924.57.

(Sgd.) C. Rogers Arundell, Member U. S. Board of Tax Appeals. (Seal.)

Certificate to foregoing paper omitted in printing.

[fol. 57] BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No., 10658

FREDERICK C. RENZIEHAUSEN, Appellant,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

EXCEPTIONS TO FINDINGS OF FACT AND CONCLUSIONS OF LAW—Filed March 7, 1927

And Now, to wit, —— —, 1928, comes the petitioner by his attorney, W. A. Seifert, and files the following exceptions to the findings of fact and conclusions of law of the

United States Board of Tax Appeals in the above-entitled case:

1. The learned Board erred in refusing to find as a fact that:

"The distilling business was a stable business. It required a great many years to build it up and get the confidence of the public, to which its product was sold. As much as two or three generations were required to build up such a business."

as requested by petitioner in his request for findings of fact No. 13.

2. The learned Board erred in refusing to find as a fact that:

"Prior to and subsequent to March 1, 1913, The Large Distilling Company's business was rapidly expanding. The reputation of Large whiskey in the trade and its standing [fol. 58] with the consumers was the very highest. The selling price per gallon of Large Whiskey in bond was always higher than that of any other rye whiskey."

as requested by petitioner in his request for findings of fact No. 16.

3. The learned Board erred in refusing to find as a fact that:

"On March 1, 1913, 5 per cent. was a fair return on the tangible property invested in The Large Distilling Company and 10 per cent. was a fair return on the intangibles in that business."

as requested by petitioner in his request for findings of fact No. 18.

4. The learned Board erred in refusing to find as a fact that:

"The March 1, 1913 value of the trade-marks, trade brands, trade names, goodwill, etc., of The Large Distilling Company was at least $1,000,000.00."

as requested by petitioner in his request for findings of fact No. 19.

5. The learned Board erred in refusing to find as a fact that:

"The value of the trade-marks, trade brands, trade names, goodwill, etc., of the firm of Schuetz, Renziehausen & Company on March 1, 1913, capitalized on the basis of 5 per cent. and 10 per cent. was $115,500.00."

as requested by petitioner in his request for findings of fact No. 23.

6. The learned Board erred in refusing to find as a fact that:

[fol. 59] "By January 31, 1918, it was certain that the Constitutional amendment would be ratified. It became effective the 16th day of January, 1920."

as requested by petitioner in his request for findings of fact No. 24.

7. The learned Board erred in refusing to find as a fact that:

"The value of the trade-marks, trade brands, trade names, good will, etc., of The Large Distilling Company as of March 1, 1913, was entirely wiped out by the Constitutional Amendment and the passage of the Willis-Campbell Act."

as requested by petitioner in his request for findings of fact No. 26.

8. The learned Board erred in refusing to find as a fact that:

"The obsolescence of the March 1, 1913, value of the trade-marks, trade brands, trade names, good will, etc., of The Large Distilling Company occurred over the period January 31, 1918, to November 30, 1921, inclusive."

as requested by petitioner in his request for findings of fact No. 29.

9. The learned Board erred in refusing to find as a fact that:

"The obsolescence of the March 1, 1913, value of the trade-marks, trade brands, trade names, good will, etc., of

the firm of Schuetz, Renziehausen & Company occurred over the period January 31, 1918, to January 16, 1920."

as requested by petitioner in his request for findings of fact No. 32.

[fol. 60] 10. The learned Board erred in refusing to find as a fact that:

"These services (petitioner's services for twenty-nine years) had a total value of $435,000.00, all of which was properly the cost of developing the good will of the company."

as requested by petitioner in his request for findings of fact No. 34.

11. The learned Board erred in refusing to find as a fact that the cost of services of petitioner was properly a cost of developing the good will of the company, as requested by petitioner in his request for findings of fact No. 35.

12. The learned Board erred in refusing to find as a fact that the physical property of The Large Distilling Company, which became obsolete over the period January 31, 1918, to November 30, 1921, had a value of $257,277.79, and that such obsolescence should be spread as follows:

1918 for 11 ms	$61,522.95
1919 " 12 "	67,115.94
1920 " 12 "	67,115.95
1921 " 11 "	61,522.95

as requested by petitioner in his request for findings of fact Nos. 37 and 38.

13. The learned Board erred in refusing to find as a fact that:

"The 'Old Whiskey' was not stock in trade, or other property which would properly be included in the inventory of the petitioner, but it was property held by the petitioner for profit and investment."

[fol. 61] as requested by petitioner in his request for findings of fact No. 40.

14. The learned Board erred in refusing to find as a fact that:

"'Old Whiskey' was not a part of The Large Distilling Company's inventory or stock in trade. The trade of The Large Distilling Company had been wiped out by the enactment of the Constitutional Amendment. The business ceased to exist. The petitioner had no alternative. He was not in a position to carry on a like business. He was forced to liquidate."

as requested by petitioner in his requests for findings of fact No. 41.

15. The learned Board erred in finding as a fact that the cost of the physical properties of The Large Distilling Company, exclusive of land, as of January 1, 1918, was $329,681.24.

16. The learned Board erred in finding as a fact that:

"In 1922 all the whiskey then carried in this account ('Old Whiskey') was sold."

17. The learned Board erred in failing and refusing to conclude as a matter of law that:

"The petitioner is entitled under Sections 214 (a) (8) of the Revenue Acts of 1918 and 1921 to deductions from gross income for the years 1918, 1919, 1920 and 1921 for obsolescence of the March 1, 1913 value of trade-marks, trade brands, trade names, good will, etc., of The Large Distilling Company."

as requested by petitioner in his request for conclusions of Law No. 1.

[fol. 62] 18. The learned Board erred in failing and refusing to conclude as a matter of law that:

"The petitioner is entitled under Sections 214 (a) (8) of the Revenue Acts of 1918 and 1921 to deductions from gross income for the years 1918, 1919, 1920 and 1921 for obsolescence of the March 1, 1913 value of trade-marks, trade brands, trade names, good will, etc., of the firm of Schuetz, Renziehausen & Company."

as requested by petitioner in his request for conclusions of law No. 2.

19. The learned Board erred in failing and refusing to conclude as a matter of law that:

"The petitioner is entitled under Sections 214 (a) (8) of the Revenue Acts of 1918 and 1921 to deductions from gross income for the years 1918, 1919, 1920 and 1921 for obsolescense of plant and equipment of The Large Distilling Company."

as requested by petitioner in his request for conclusions of law No. 3.

20. The learned Board erred in failing and refusing to conclude as a matter of law that:

"The petitioner is entitled under Section 206 of the Revenue Act of 1921 to have The Large Distilling Company's net income for the year 1922 taxed at the rate of 12½%."

as requested by petitioner in his request for conclusions of law No. 4.

21. The learned Board erred in failing and refusing to conclude as a matter of law that:

"The petitioner is entitled under Section 214 (a) (8) of the Revenue Act of 1918 to a deduction from gross income [fol. 63] for the year 1919 of the cost of the trade-marks, trade brands, trade names, good will, etc., of The Large Distilling Company destroyed by the ratification of the Eighteenth Amendment of January 16, 1919."

as requested by petitioner in his alternate request for conclusions of Law No. 1.

22. The learned Board erred in concluding as a matter of law that:

"The mere ratification of the Eighteenth Amendment did not destroy the business of The Large Distilling Company or render its intangibles obsolete, for it continued to carry on the business after January 16, 1919, and after the Eighteenth Amendment and enforcement legislation became

effective in 1920, under the same trade-marks, trade name, and trade brand, although modified somewhat as to methods by reason of such legislation. Prior to 1919 The Large Distilling Company sold its product before it was manufactured to the wholesale liquor trade and made delivery in bulk in an unmatured state at its bonded warehouses. Beginning with 1919 its whiskey was matured in bonded ware houses, bottled in bond, and disposed of to the wholesale and retail drug trade or others holding Government permits. As late as 1922, the last year we have for review, The Large Distilling Company was still disposing of its whiskey stock under the same trade-marks, trade name and trade brands, and there is no record evidence as to when, if at all, the business was finally terminated. Prohibition *w*rought changes in the method of doing business and in the character of its clientele, but the business which it carried on both before and after prohibition became effective, and throughout all of the years under review, was essentially the same. We see no proper grounds upon which to base a deduction for 1919 or any other year on appeal for obsoleteness of intangibles of The Large Distilling Company."

[fol. 64] 23. The learned Board erred in concluding as a matter of law:

"Under the circumstances of this case it cannot be held that the tangible assets of The Large Distilling Company were in a state or condition of becoming obsolete in 1918, 1919 or 1920. Renziehausen thought he was through in 1918, but his convictions were based upon a lack of knowledge of his lawful rights; and in 1919 he resumed distilling operations and continued to carry on such operations until the enactment of the Willis-Campbell Act on or about November 23, 1921. The plant facilities of The Large Distilling Company were being used at the close of 1919 and 1920 for the purposes for which they had been acquired, and apparently without any diminution as to usage prior to prohibition legislation. It was the passage of the Willis-Campbell Act in 1921 which prohibited the manufacture of medicinal whiskey except under permits issued by the Commissioner of Internal Revenue, and the continued refusal of that officer to issue such permits, which forced the peti-

tioner to discontinue distilling operations and rendered the plant facilities of The Large Distilling Company, other than its bonded warehouses, obsolete; and this event could not have been foreseen in 1918, 1919 or 1920. As Renziehausen testified, the passage of the Willis-Campbell Act came suddenly, like a bolt out of a clear sky, and he did not at the time consider the passage of that Act possible. We find no error in respondent's refusal to allow deductions from the income of 1918, 1919 and 1920 for obsolescence of the tangible properties of The Large Distilling Company. As to 1921, we think obsoleteness of the tangible properties, other than the bonded warehouses, took place wholly within that year, by virtue of the enactment of the Willis-Campbell Act and the continued refusal of the Commissioner of Internal Revenue to issue permits, under that Act, for the manufacture of medicinal whiskey. As to the amount of the deduction for that year, we leave that for determination under the next issue."

[fol. 65] 24. The learned Board erred in concluding as a matter of law:

"Renziehausen, for he and The Large Distilling Company are the same person, was engaged in the business of distilling and selling whiskey, and as incidents to the conduct of such business, he bought and sold the product of his own plant whenever warehouse receipts were available for purchase, and he matured the excess of each season's production and sold it to the trade. The petitioner was engaged in more than a distilling business; he was also trading in whiskey. Whiskey was his stock in trade. Beginning in 1908, the excess production of each distilling season was charged on the books of The Large Distilling Company to the 'Old Whiskey' account. As this whiskey matured, or perhaps in some cases prior to complete maturity, the whiskey was sold by, and through the organization of The Large Distilling Company. It is not in evidence whether the profits from the sale of this whiskey, as sales were made in prior years, were included in the earnings of The Large Distilling Company, or withdrawn by the petitioner, or credited to his account. The whiskey sold in 1922 was a part of the whiskey carried in this account and represented the accumulation of excess production of several distilling

seasons. It was property of a kind which would properly have been included in the petitioner's inventory, had it been on hand at the close of the year 1922, and, therefore, does not come within the statutory definition of capital assets.

"Petitioner makes the alternative contention that all of the income of The Large Distilling Company for 1922 should be treated as capital gain, since the business was being liquidated from November, 1921, and the inventory became a frozen capital asset when liquidation began. But neither does this contention appear to us to be tenable. Whatever stock in trade The Large Distilling Company had on hand when liquidation commenced continued to be inventoriable [fol. 66] stock in trade until disposed of. Its character was not in the least changed because of the fact that the business was in process of liquidation. We find no error in respondent's action in refusing to treat the profit derived from the sale of old whiskey in 1922 as a capital gain."

25. The learned Board erred in entering an order of redetermination.

—— ——, Attorneys for Appellant.

And now, to wit, —— —, 1928, exception is hereby noted to each of the above twenty-five exceptions and bills sealed.

—— ——, Member United States Board of Tax Appeals.

Now, July 24, 1928, the foregoing exceptions to findings of fact and conclusions of law certified from the record as a true copy.

B. D. Gamble, Clerk U. S. Board of Tax Appeals.
(Seal.)

[fol. 67] AFFIDAVIT

WASHINGTON,
District of Columbia, ss:

Anthony C. DeMott, being first duly sworn, says: I am a citizen of the United States of America; over the age of twenty-one; and not a party to, or in any way interested in, the proceedings in which these exceptions were taken.

That on the seventh day of March, 1928, I served the original of the annexed exceptions to findings of fact and conclusions of law on Mr. Roger C. Arundell, member of the United States Board of Tax Appeals, Earle Building, Washington, D. C., and requested that he sign them, and that he refused to do so.

The original was then left with the board and a copy thereof was served on Mr. J. W. Foley, special attorney of the general counsel of the Bureau of Internal Revenue in the Walker-Johnson Building, Washington, D. C.

Anthony C. DeMott.

Sworn to and subscribed before me this 7th day of March, 1928. Veshena A. Tompkins, Notary Public. My commission expires July 24, 1929. (Seal.)

Now, July 24, 1928, the foregoing affidavit of service of exceptions certified from the record as a true copy.

B. D. Gamble, Clerk U. S. Board of Tax Appeals. (Seal.)

[fol. 68] Before United States Board of Tax Appeals

Docket No., 10658

Frederick C. Renziehausen, Appellant,

v.

Commissioner of Internal Revenue, Respondent

Petitioner's Petition for Review—Filed March 9, 1928

To the Honorable the Members of the United States Board of Tax Appeals:

The petition of Frederick C. Renziehausen, appellant, for review of the final decision of the United States Board of Tax Appeals, entered September 17, 1927, in the above-entitled case, respectfully represents:

First. The petitioner is a citizen and resident of the City of Pittsburgh, County of Allegheny and State of Pennsylvania.

Second. That the nature of the controversy is the determination of deficiencies in income taxes for the calendar years 1918 to 1922, inclusive. The petitioner claimed as deductions in computing net income of the respective years the following:

(a) Obsolescence of intangibles consisting of trademarks, trade brands, trade names, good-will, etc., of The Large Distilling Company, under which name he had been transacting business, and of Schuetz, Renziehausen & Company, of which he was a partner, or that if he were not entitled to such obsolescence he claimed a deduction of [fol. 69] $578,281.12 in the year 1919, based upon loss of the cost of such intangibles.

(b) Obsolescence of plant and equipment of The Large Distilling Company spread over the years 1918, 1919, 1920 and 1921, or that if he were not entitled to such obsolescence he claimed deductions for depreciation sustained in the said years and a deduction for loss of useful value of plant and equipment in the year 1921.

The petitioner also claimed that the income realized from the sale of "Old Whiskey" during 1922 should be taxed at the rate of 12½ per centum, and not at the ordinary income and surtax rates, on the grounds that the "Old Whiskey" was a personal investment of the petitioner and, in the alternative, that all stock in trade or inventory became a capital asset upon the cessation of the usual course of business and the beginning of liquidation, whether voluntary or involuntary.

The board allowed deduction for depreciation sustained in the years 1918, 1919, 1920 and 1921 and for loss of useful value or obsoleteness of plant and equipment, except bonded warehouses for the year 1921, and refused to allow the deductions for obsolescence of intangibles, or to permit the spread of the obsolescence of the plant and equipment over the years 1918, 1919, 1920 and 1921, and held that the income realized from the liquidation of the assets of The Large Distilling Company should be taxed at the ordinary income and surtax rates, and not at the capital gain rate.

Third. That review of said final decision is sought in the United States Circuit Court of Appeals for the Third Circuit.

Fourth. That your petitioner makes the following assignments of error:

[fol. 70] 1. The learned Board erred in refusing to find as a fact that:

"The distilling business was a stable business. It required a great many years to build it up and get the confidence of the public, to which its product was sold. As much as two or three generations were required to build up such a business."

as requested by petitioner in his request for findings of fact No. 13.

2. The learned Board erred in refusing to find as a fact that:

"Prior to and subsequent to March 1, 1913, The Large Distilling Company's business was rapidly expanding. The reputation of Large Whiskey in the trade and its standing with the consumers was the very highest. The selling price per gallon of Large Whiskey in bond was always higher than that of any other rye whiskey."

as requested by petitioner in his request for findings of fact No. 16.

3. The learned Board erred in refusing to find as a fact that:

"On March 1, 1913, 5 per cent was a fair return on the tangible property invested in The Large Distilling Company and 10 per cent was a fair return on the intangibles in that business."

as requested by petitioner in his request for findings of fact No. 18.

4. The learned Board erred in refusing to find as a fact that:

"The March 1, 1913 value of the trade-marks, trade brands, trade names, good-will, etc., of The Large Distilling Company was at least $1,000,000.00."

[fol. 71] as requested by petitioner in his request for findings of fact No. 19.

5. The learned Board erred in refusing to find as a fact that:

"The value of the trade-marks, trade brands, trade names, good-will, etc., of the firm of Schuetz, Renziehausen & Company on March 1, 1913, capitalized on the basis of 5 per cent and 10 per cent was $115,500.00."

as requested by petitioner in his request for findings of fact No. 23.

6. The learned Board erred in refusing to find as a fact that:

"By January 31, 1918, it was certain that the Constitutional Amendment would be ratified. It became effective the 16th day of January, 1920."

as requested by petitioner in his request for findings of fact No. 24.

7. The learned Board erred in refusing to find as a fact that:

"The value of the trade-marks, trade brands, trade names, good-will, etc., of The Large Distilling Company as of March 1, 1913, was entirely wiped out by the Constitutional Amendment and the passage of the Willis-Campbell Act."

as requested by petitioner in his request for findings of fact No. 26.

8. The learned Board erred in refusing to find as a fact that:

"The obsolescence of the March 1, 1913 value of the trade-marks, trade brands, trade names, good-will, etc., of The Large Distilling Company occurred over the period January 31, 1918 to November 30, 1921, inclusive."

[fol. 72] as requested by petitioner in his request for findings of fact No. 29.

9. The learned Board erred in refusing to find as a fact that:

"The obsolescence of the March 1, 1913 value of the trade-marks, trade brands, trade names, good-will, etc., of

the firm of Schuetz, Renziehausen & Company occurred over the period January 31, 1918 to January 16, 1920."

as requested by petitioner in his request for findings of fact No. 32.

10. The learned Board erred in refusing to find as a fact that:

"These services (petitioner's services for twenty-nine years) had a total value of $435,000.00, all of which was properly the cost of developing the good-will of the company."

as requested by petitioner in his request for findings of fact No. 34.

11. The learned Board erred in refusing to find as a fact that the cost of services of petitioner was properly a cost of developing the good-will of the company, as requested by petitioner in his request for findings of fact No. 35.

12. The learned Board erred in refusing to find as a fact that the physical property of The Large Distilling Company, which became obsolete over the period January 31, 1918, to November 30, 1921, had a value of $257,277.79, and that such obsolescence should be spread as follows:

1918 for 11 months	$61,522.95
1919 " 12 "	67,115.94
1920 " 12 "	67,115.95
1921 " 11 "	61,522.95

[fol. 73] as requested by petitioner in his request for findings of fact Nos. 37 and 38.

13. The learned Board erred in refusing to find as a fact that:

"The 'Old Whiskey' was not stock in trade, or other property which would properly be included in the inventory of the petitioner, but it was property held by the petitioner for profit and investment."

as requested by petitioner in his request for findings of fact No. 40.

14. The learned Board erred in refusing to find as a fact that:

"'Old Whiskey' was not a part of The Large Distilling Company's inventory or stock in trade. The trade of The Large Distilling Company had been wiped out by the enactment of the Constitutional amendment. The business ceased to exist. The petitioner had no alternative. He was not in a position to carry on a like business. He was forced to liquidate."

as requested by petitioner in his request for findings of fact No. 41.

15. The learned Board erred in finding as a fact that the cost of the physical properties of The Large Distilling Company, exclusive of land, as of January 1, 1918, was $329,-681.24.

16. The learned Board erred in finding as a fact that:

"In 1922 all of the whiskey then carried in this account ('Old Whiskey') was sold."

17. The learned Board erred in failing and refusing to conclude as a matter of law that:

[fol. 74] "The petitioner is entitled under Sections 214 (a) (8) of the Revenue Acts of 1918 and 1921 to deductions from gross income for the years 1918, 1919, 1920 and 1921 for obsolescence of the March 1, 1913 value of trade-marks, trade brands, trade names, goodwill, etc., of The Large Distilling Company."

as requested by petitioner in his request for conclusions of law No. 1.

18. The learned Board erred in failing and refusing to conclude as a matter of law that:

"The petitioner is entitled under Sections 214 (a) (8) of the Revenue Acts of 1918 and 1921 to deductions from gross income for the years 1918, 1919, 1920 and 1921 for obsolescence of the March 1, 1913 value of trade-marks, trade brands, trade names, goodwill, etc., of the firm of Schuetz, Renziehausen & Company."

as requested by petitioner in his request for conclusions of law No. 2.

19. The learned Board erred in failing and refusing to conclude as a matter of law that:

"The petitioner is entitled under Sections 214 (a) (8) of the Revenue Acts of 1918 and 1921 to deductions from gross income for the years 1918, 1919, 1920 and 1921 for obsolescence of plant and equipment of The Large Distilling Company."

as requested by petitioner in his request for conclusions of law No. 3.

20. The learned Board erred in failing and refusing to conclude as a matter of law that:

"The petitioner is entitled under Section 206 of the Revenue Act of 1921 to have The Large Distilling Company's net income for the year 1922 taxed at the rate of 12½%."

[fol. 75] as requested by petitioner in his request for conclusions of law No. 4.

21. The learned Board erred in failing and refusing to conclude as a matter of law that:

"The petitioner is entitled under Section 214 (a) (8) of the Revenue Act of 1918 to a deduction from gross income for the year 1919 of the cost of the trade-marks, trade brands, trade names, goodwill, etc., of The Large Distilling Company destroyed by the ratification of the Eighteenth Amendment on January 16, 1919."

as requested by petitioner in his alternate request for conclusions of Law No. 1.

22. The learned Board erred in concluding as a matter of law that:

"The mere ratification of the Eighteenth Amendment did not destroy the business of The Large Distilling Company or render its intangibles obsolete, for it continued to carry on the business after January 16, 1919, and after the Eighteenth Amendment and enforcement legislation became effective in 1920, under the same trade-marks, trade name, and trade brand, although modified somewhat as to methods by reason of such legislation. Prior to 1919 The Large Distilling Company sold its product before it was manufactured to the wholesale liquor trade and made delivery in bulk in an unmatured state at its bonded warehouses. Be-

ginning with 1919 its whiskey was matured in bonded warehouses, bottled in bond, and disposed of to the wholesale and retail drug trade or others holding Government permits. As late as 1922, the last year we have for review, The Large Distilling Company was still disposing of its whiskey stock under the same trade-marks, trade name and trade brands, and there is no record evidence as to when, if at all, the business was finally terminated. Prohibition wrought changes in the method of doing business and in the [fol. 76] character of its clientele, but the business which it carried on both before and after prohibition became effective, and throughout all of the years under review, was essentially the same. We see no proper grounds upon which to base a deduction for 1919 or any other year on appeal for obsoleteness of intangibles of The Large Distilling Company."

23. The learned Board erred in concluding as a matter of law:

"Under the circumstances of this case it can not be held that the tangible assets of The Large Distilling Company were in a state or condition of becoming obsolete in 1918, 1919 or 1920. Renziehausen thought he was through in 1918, but his convictions were based upon a lack of knowledge of his lawful rights; and in 1919 he resumed distilling operations and continued to carry on such operations until the enactment of the Willis-Campbell Act on or about November 23, 1921. The plant facilities of The Large Distilling Company were being used at the close of 1919 and 1920 for the purposes for which they had been acquired, and apparently without any diminution as to usage prior to prohibition legislation. It was the passage of the Willis-Campbell Act in 1921 which prohibited the manufacture of medicinal whiskey except under permits issued by the Commissioner of Internal Revenue, and the continued refusal of that officer to issue such permits, which forced the petitioner to discontinue distilling operations and rendered the plant facilities of The Large Distilling Company, other than its bonded warehouses, obsolete; and this event could not have been foreseen in 1918, 1919 or 1920. As Renziehausen

testified, the passage of the Willis-Campbell Act came suddenly, like a bolt out of a clear sky, and he did not at the time consider the passage of that Act possible. We find no error in respondent's refusal to allow deductions from the income of 1918, 1919 and 1920 for obsolescence of the tangible properties of The Large Distilling Company. As [fol. 77] to 1921, we think obsoleteness of the tangible properties, other than the bonded warehouses, took place wholly within that year, by virtue of the enactment of the Willis-Campbell Act and the continued refusal of the Commissioner of Internal Revenue to issue permits, under that Act, for the manufacture of medicinal whiskey. As to the amount of the deduction for that year, we leave that for determination under the next issue."

24. The learned Board erred in concluding as a matter of law:

"Renziehausen, for he and The Large Distilling Company are the same person, was engaged in the business of distilling and selling whiskey, and as incidents to the conduct of such business, he bought and sold the product of his own plant whenever warehouse receipts were available for purchase, and he matured the excess of each season's production and sold it to the trade. The petitioner was engaged in more than a distilling business; he was also trading in whiskey. Whiskey was his stock in trade. Beginning in 1908, the excess production of each distilling season was charged on the books of The Large Distilling Company to the 'Old Whiskey' account. As this whiskey matured, or perhaps in some cases prior to complete maturity, the whiskey was sold by, and through the organization of The Large Distilling Company. It is not in evidence whether the profits from the sale of this whiskey, as sales were made in prior years, were included in the earnings of The Large Distilling Company, or withdrawn by the petitioner, or credited to his account. The whiskey sold in 1922 was a part of the whiskey carried in this account and represented the accumulation of excess production of several distilling seasons. It was property of a kind which would properly have been included in the petitioner's inventory had it been on hand at the close of the year 1922, and, therefore, does not come within the statutory definition of capital assets.

[fol. 78] "Petitioner makes the alternative contention that all of the income of The Large Distilling Company for 1922 should be treated as capital gain, since the business was being liquidated from November, 1921, and the inventory became a frozen capital asset when liquidation began. But neither does this contention appear to us to be tenable. Whatever stock in trade The Large Distilling Company had on hand when liquidation commenced continued to be inventoriable stock in trade until disposed of. Its character was not in the least changed because of the fact that the business was in process of liquidation. We find no error in respondent's action in refusing to treat the profit derived from the sale of old whiskey in 1922, as a capital gain."

25. The learned Board erred in entering an order of redetermination.

26. The learned Board erred in refusing to grant petitioner an exception to each of the above assignments of error, and in refusing to seal a bill therefor.

Wherefore your petitioner prays that the United States Circuit Court of Appeals for the Third Circuit may review the action of the Board of Tax Appeals in this cause, reverse the decision of the Board and direct the entry of a decision by said Board in favor of the petitioner, determining that the deductions claimed for the years 1918, 1919, 1920 and 1921 be allowed and that the income for the year 1922 be taxed at the capital gain rate of 12½ per centum, or for such other and further relief as may to the Court appear proper in the premises.

W. A. Seifert, Smith, Shaw & McClay, Attorneys for Appellant.

[fol. 79] *Duly sworn to by F. C. Renziehausen. Jurat omitted in printing.*

Certificate to foregoing paper omitted in printing.

[fol. 80] BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No., 10658

FREDERICK C. RENZIEHAUSEN, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

RESPONDENT'S PETITION FOR REVIEW IN THE UNITED STATES CIRCUIT COURT OF APPEALS AND ASSIGNMENT OF ERRORS—Filed May 31, 1928

Now comes David H. Blair, commissioner of internal revenue, by his attorneys, Mabel Walker Willebrandt, assistant attorney general, and C. M. Charest, general counsel, Bureau of Internal Revenue, and respectfully shows:

I. That he is the duly appointed, qualified, and acting commissioner of internal revenue, appointed and holding his office by virtue of the laws of the United States; that Frederick C. Renziehausen, an individual taxpayer subject to the provisions of the Revenue Act of 1921 is, and was throughout the taxable years 1921 and 1922, an inhabitant of the City of Pittsburgh, Allegheny County, Pennsylvania, which is within the jurisdiction of the United States Court of Appeals of the Third Circuit.

II. That the nature of the controversy is as follows, to wit:

The question is whether 1921 and 1922 deductions from gross income are allowable to the said taxpayer because of obsoleteness or obsolescence or loss of useful value of cer- [fol. 81] tain distillery buildings, equipment, and warehouses.

In the year 1921, and for many years prior thereto, the taxpayer was the sole owner of a whiskey distilling business conducted under the trade name of Large Distilling Company, and of certain buildings, equipment and warehouses used in connection therewith.

Shortly prior to the effective date of the Eighteenth Amendment the taxpayer discontinued the distillation of whiskey, but on and after that date continued to employ

his warehouses in the storage of whiskey previously distilled. Beginning in the fall of 1919, and continuing up to November 23, 1921, he engaged in the distillation and storage of medicinal whiskey.

On November 23, 1921, the so-called Willis-Campbell Act was approved prohibiting the manufacture of medicinal whiskeys without a permit in that respect such as was authorized by the act to be issued by the Commissioner of Internal Revenue. No such permits have ever been issued, the existing stock of whiskeys being adequate to meet all medicinal requirements.

The taxpayer's warehouses were of such construction that they were valuable only for the storage of whiskey in bulk. They had a total capacity of 55,000 barrels. On November 23, 1921, the taxpayer had stored in those warehouses 27,393 barrels of whiskey. Of that number, 1,761 barrels were removed during 1922. There were no replacements.

The said commissioner had refused to allow to the said taxpayer any deduction based upon the alleged obsoleteness or obsolescence of his said facilities, and notified the said taxpayer of this determination of and of his proposal to assess 1921 and 1922 income tax deficiencies in the respective amounts of $83,028.63 and $69,752.49.

From the determination of the said commissioner, the said taxpayer appealed to the United States Board of Tax [fol. 82] Appeals, and the board held that due to the enactment of the Willis-Campbell Act on November 23, 1921, and the subsequent refusal of the Commissioner of Internal Revenue to issue permits for the manufacture of medicinal whiskey, a total obsoleteness and loss of useful value of the taxpayer's plant and equipment, other than warehouses, resulted in 1921, and directed the allowance of a 1921 deduction computed accordingly. The Board further held that obsolescence of the taxpayer's warehouses set in on November 23, 1921, and directed the allowance of 1921 and 1922 deductions with respect thereto. The Board accordingly held that there was no 1921 deficiency, but, on the contrary, that there existed an overassessment for the year 1921 in the amount of $23,924.57; the Board further held that a 1922 deficiency existed only in the amount of $67,745.39.

The hearing before the Board was held on December 13, 1926. The interlocutory decision of the Board and its find-

ings of fact and opinion were promulgated on September 17, 1927. The final order of redetermination was entered on December 14, 1927.

III. That said Commissioner, being aggrieved by the conclusions of law contained in said decision and by the said order of redetermination, desires to obtain a review thereof by the United States Circuit Court of Appeals for the Third Circuit: Wherefore, he petitions that a transcript of record be prepared in accordance with the rules of the United States Circuit Court of Appeals for the Third Circuit and transmitted to the Clerk of said Court for filing and appropriate action to the end that the errors complained of may be reviewed and corrected by the said United States Circuit Court of Appeals for the Third Circuit.

IV. That said Commissioner's assignments of error are as follows:

[fol. 83] 1. The Board of Tax Appeals erred in holding that the tangible property of the Large Distilling Company, other than its warehouses was rendered entirely obsolete by virtue of the enactment of the Willis-Campbell Act.

2. The Board erred in holding that obsolescence of the warehouses of the Large Distilling Company set in as a result of the enactment of the Willis-Campbell Act.

3. The Board erred in holding that the taxpayer was entitled to a 1921 deduction based upon the obsoleteness of the tangible property, other than warehouses, of the Large Distilling Company.

4. The Board erred in holding that the taxpayer was entitled to a 1921 deduction based upon loss of useful value of the tangible property, other than warehouses, of the Large Distilling Company.

5. The Board erred in holding that the taxpayer was entitled to 1921 and 1922 deductions based upon obsolescence of the warehouses of the Large Distilling Company.

6. The Board erred in holding that there existed an overassessment for the taxable year 1921.

7. The Board erred in failing and refusing to approve the 1921 and 1922 deficiencies as determined by the Commissioner.

Mabel Walker Willebrandt, Assistant Attorney General. C. M. Charest, General Counsel, Bureau of Internal Revenue. Of Counsel: V. J. Heffernan, Special Attorney, Bureau of Internal Revenue.

[fol. 84] *Duly sworn to by C. M. Charest. Jurat omitted in printing.*

Certificate to foregoing paper omitted in printing.

[fol. 85] BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No., 10658

FREDERICK C. RENZIEHAUSEN, Appellant,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Condensed Statement of the Evidence Material to Issues— Filed July 16, 1928

APPELLANT'S EVIDENCE

FREDERICK CHRISTIAN RENZIEHAUSEN, the appellant, on oath, testified in substance as follows:

The nature and character of the distilling business was stable because you could sell your goods, conduct your business in an orderly manner and make money. It is as stable as any business I could say.

It would take a great many years to build up a distilling business, to get the confidence of the public to whom you wanted to sell your product. That takes two or three generations. It has been taking two or three generations to do that on any brand that I am familiar with. It would take many years to build up a reputation and standing on an article like whiskey, that the consumer buys for his stomach. You must know something about it. That is the history of the distilling business. They have not been able to build it

up in a short time. It takes years and years. I have in mind such brands as A. Overholt & Company established in 1810. Gibson, I think, was established in 1840. All [fol. 86] brands of rye whiskey in our territory, wherever I know of them, have been two or three generations in establishing. The distillation of rye whiskey was produced in the states of Pennsylvania and Maryland. There was no reputation for rye whiskey anywhere outside of those two states, for the manufacture. There was stability to my business. We had a good standing wherever we were known, wherever we tried to do business. The wholesale trade had confidence in our firm. The consumers liked our product. It was a stable business, stable as the word would apply in connection with any business.

For the year 1913 and for some years prior thereto, we invariably had our whiskeys all sold before it was produced on contract. We could have sold a larger amount than our product. The same condition continued after March 1, 1913, up until the enactment of the National Prohibition Law. The demand after March 1, 1913, increased continually until the spring of 1917 and that season we foresaw to some extent that prohibition might come, and that is the last beverage whiskey we distilled, in May, 1917.

On March 1, 1913, I considered 5% a fair return or interest rate on the tangible property invested in my business and 10% a fair return on the goodwill value of my business.

Assuming that the value of my plant averaged over a period from June 30, 1908, to June 30, 1912, approximately $251,000.00, and that my earnings for the years ending June 30, 1909, 1910, 1911, 1912 and 1913 approximated $85,000.00 averaged over that period, and considering the stability of the whiskey business generally and my knowledge of my own business, the stability of that business and the future prospects, I figure that the goodwill of the Large Distilling Company on March 1, 1913, was worth at least $1,000,000.00.

[fol. 87] The goodwill is an invisible asset. It is there. It brings business. It is invisible. It was in beverage days in our case, and at that time I considered that it was worth that amount and it was growing, growing, growing, and I believe would have been worth a great deal more in a few years. The earnings continued to increase after March

1, 1913. In arriving at the value of the goodwill to trademarks and trade names as of March 1, 1913, I considered that it takes time to build up an established brand of whiskey, to get goodwill. I considered that the Large Distilling Company was started as far back as 1796. I considered the whole situation.

Anybody that had brains enough to go in the distilling business would buy something that had a reputation. You usually buy out a brand and resurrect an old name in the distilling business. He wouldn't build a distillery first because he could not have any goodwill. He would not be known and he would have to sell his product in competition with the closest sold goods. He would either have to sell at a lower price than other brands or he would not make any headway. People would not tie up their money for four years in whiskey unless they could see the money coming back with a profit. The goodwill of the Large Distilling Company after March 1, 1913, continually grew in value.

The Constitutional Amendment became effective on January 16, 1920. Thereafter, we could sell whiskey only on permit. We would have to have a basic permit and sell only to those that held Government permits. It restricted our business. Our customers were not the same after January 16, 1920, as before. We lost all our customers in the beverage trade. They were all gone and we had to build up any trade for medical purposes.

[fol. 88] We manufactured 16,700 and some odd barrels of whiskey from the fall of 1919 up to the fall of 1921 for medicinal purposes. We did not have a permit. We just manufactured whiskey because we exercised a right that we had. We conferred with Commissioner Roper about the amount of the bond. Since the spring of 1921 we have not manufactured any whiskey for medicinal or beverage purposes subsequent to the fall of 1921. Since November 21, 1921, nobody has received a permit to manufacture any whiskey in this country.

Our business is now in liquidation and has been since the fall of 1921. In 1918 we thought the business would be wound up in a period of about four years. The Amendment had been passed to be effective in 1920. We did not know in what form it was in, but we knew the distilling business would have to be wound up until we later changed

our minds and thought we had a right which we would exercise. In 1918 we thought we would have to wind up the whole business, that the warehouses would become empty in about four years and the thing was empty. There was some whiskey in bond and none was being produced. We thought it would be withdrawn rapidly and ours would go out of the warehouse the same as every other distillery. Our opinion was the whole thing would go on an alcohol basis, and that is about what it has done.

We had an account called "Old Whiskey," which represented an investment made in whiskeys carried into it. The production at the end of the distilling season that was not sold or delivered on contracts, we manufactured and carried in there as an investment by me. The whiskey that was sold in 1922 had been carried in that account for four or five years. None of it had been carried less than two years. I carried a number of my personal investments in the books of the Large Distilling Company, prior to and [fol. 89] after the "Old Whiskey" account was opened and am still carrying them there.

When whiskey was distilled and placed in bonded warehouses we gave a warehouse receipt as evidence of the title and ownership of that whiskey. The warehouse receipts were issued in the name of the purchaser or contractor. They could be sold. They were negotiable. They were good collateral and bankers considered them favorably and would loan on them as freely as on certificates for pig iron or any other kind of material for which warehouse receipts may be issued by storage companies.

I was the sole owner of the business and for convenience I carried a large part of my personal investments on the books of the Large Distilling Company. I treated it all as my own individual affair.

My stock in trade consisted of grain, rye and barley malt, empty whiskey barrels, cooperage supplies, supplies for the bottling house, material of that kind and everything else required by a distillery to manufacture whiskey. Automobiles were carried in the books of account. I don't recall whether we carried anything else in inventory for the purpose of determining profit.

Schuetz-Renziehausen & Company on March 1, 1913, sold its goods principally to licensed retail liquor dealers, saloon

keepers. It also had a floor trade, bottled goods sold to family trade. We enjoyed some of the most substantial retailers there were in our community in the territory in which we did business, hotel keepers and a good class of people.

Assuming that at the beginning of the years 1908 to 1912 we had tangible assets which for that five-year period averaged approximately $309,000.00 and that the income from the partnership for those years was approximately $27,000.00 odd, in my opinion the March 1, 1913, value of the goodwill, trade-marks and trade brands of Schuetz-Renzie- [fol. 90] hausen & Company was somewhere between $150,000.00 and $200,000.00.

After 1913 the sales grew. The business was more profitable, if my memory serves me right.

I arrive at that figure because it was a going business. It could have been sold at that price to somebody who wanted to engage in that business. It had a good class of trade established for many years and it had that value to anybody going into business without any trade, would not have any goodwill, but we had something there, an invisible asset, and that is what I think that asset in that particular business was worth. Of course that business was mercantile, buying and selling, but it had a run of trade that was good, that had a value.

I can't recall any other wholesale liquor dealers as firms who had been in business longer than we had except Schmidt and Friday and they had dissolved and continued in business separately.

The good will which existed on March 1, 1913, continued until it was destroyed by the Prohibition Amendment, January 16, 1920.

Cross-examination:

The Large Distilling Company had renewed since January 16, 1920, the date on which National Prohibition became effective, some of its whiskey trade-marks.

The brands of whiskey known as "Sam Thompson," "Finch Golden Wedding," "Dillinger," "Guggenheimer" were all brought out at least sixty years ago. I don't know how long it was from the time they were brought out before they were established. The brand "Large Whis-

key," which is the only brand the Large Distilling Company has, was brought out, established, founded in 1796. [fol. 91] The brand of the star within a star was brought out by Henry Large after he became the owner in 1860 or 1861.

Before prohibition we could sell all the whiskey that we made, the demand exceeded the supply. If we had produced more than we were creating a demand for by goodwill we would soon fall down. Our policy would have to be to restrict the production in accordance with the demand. We didn't try to make a little bit more of it so as to satisfy the demand somewhat more because whiskey is not a matter like white lead or a dairy product or wire nails. You can add to your plant and keep on producing whiskey, the character we made, would have to remain in bond for a period of four years to mature, and then market it, then put into consumption. You can't make the comparisons. We were not producing all the whiskey we could. Our capacity was more than we produced. We were not filled up in storage, but if we would produce our capacity we would soon fall down in the markets. The people wouldn't buy the whiskey. They would say, "I can buy that after awhile." It was a restriction of production as our goodwill was being extended, created, that it would absorb our supply at a good profit to the owner of whiskey certificates in bond. We didn't want to produce more than we could sell easily. And to have them call for it, invest their money in it, we had to make it attractive, because it took too much capital. When we made it attractive, as an investment, they put their money into it.

Tangibles are property, buildings, machinery and such things that you can make whiskey with, a plant. I consider 5 per cent a fair return on that kind of property.

A way of calculating the value of the goodwill is to take 5 per cent of the average value of the tangibles, subtract the result from the average net earnings and multiply that result by ten. Using that method you take 5 per cent of [fol. 92] $251,000 and get $12,550, which you subtract from $85,000 and get $72,450, which you multiply by ten and get $724,500 as the value of the goodwill under that formula. In arriving at a value of $1,000,000, I did in a measure attempt to work out a formula and find out what the value

was, but I included what the business and goodwill would bring in addition to what the figures showed. I knew there was an invisible goodwill value there. I figured that is worth at least $1,000,000. I think the goodwill is there for all that discrepancy and more. It was all there. I can give you nothing definite. It is invisible, but it is there. That is what I believe and know. I have grown up with it and I know it is there. The figures don't show at all the correct result. The formula don't show all the good-will value.

"Q. The formula is no good?
"A. You can't throw it away that far, in my opinion."

Prohibition was to go into effect on the 16th of January, 1920, only two years from 1918, but we had whiskey in there. We expected to sell it for medicinal purposes. That is why I thought it would take four years to wind up the distilling business.

We got to thinking about making whiskey for medicinal purposes all the time we were liquidating. Everybody, the press, the whole nation, were saying that the whiskey business was done. I can't give any day or date when it first occurred to us. I know, at first, in 1918, we decided the whole thing was up, but it later developed that it was not, but in 1918 we thought the jig was up. We commenced to manufacture for medicinal purposes in the summer and fall of 1919. We made that whiskey from the same formula. In the fall or summer of 1919, we found out that we were mistaken in the assumption in 1918 that the business would [fol. 93] have to be wound up in four years, and we kept on making whiskey until the passage of the Willis-Campbell Act. The brewers wanted to make whiskey and Senator Willis wanted to stop them and he commenced to jamb what was known as a beer bill through Congress and they put in that joker that distilleries would have to stop manufacturing whiskey, too, and we made whiskey up until the 23d. If the old brewers had stayed out we would be making whiskey today.

"Q. It was a bolt out of a clear sky, wasn't it?
"A. What is that?
"Q. That was a bolt out of a clear sky?"
"A. We did not know."

We did not think that the Republican Party would allow the Willis-Campbell Act to pass. The whole thing was in the Democratic Party, and the Republicans ought to have kept their hands off. They ought to have pulled Willis away and say "lay low."

The goodwill value in the mercantile business would not be as valuable as the goodwill in the manufacturing plant. Using the same formula as was used in the Large Distilling Company case, we take 5 per cent of $309,000 and get $15,450, which we subtract from $27,000 and get a difference of $11,550, which you multiply by ten and gives you a valuation of $115,500.

We would have asked $150,000 to $200,000 for the goodwill if we had sold it, if anybody wanted to buy it. The discrepancy between $115,500 and anywhere from $150,000 to $200,000 is because there is some invisible goodwill there that you can't see. It is there. It is worth that difference. I was valuing the goodwill with figures. There is nothing wrong that I can see with the formula. It is all right in a measure. It only applies to our business, to Schuetz, Renziehausen & Company's business. In the face of the figures, I think that goodwill was worth $150,000 [fol. 94] or $200,000. Goodwill can't be figured by figures. You can't measure everything with a yardstick. Somebody wants to sell and the other fellow thinks it is worth that and pays you for it, then it is worth that. You can offer it for sale and set a figure on it. To set a figure on it you have got to know yourself and if you can show it to the fellow, what you know, he will pay it. In a measure you have to pick it out of the air. I have bought and sold many things, but I was never governed very much by figures. I would have to use my head on that, what it is worth, a little common sense comes in there, not all figures of the books. It is a whole lot easier to sit in an office and do figures, but you don't always realize on things that way.

As far as my memory goes, the sales of Schuetz-Renziehausen & Company grew considerably after 1913. I would have to have the books to see that. We did an increased business on the floor and through our agents.

The "Old Whiskey" account referred to the Large Distilling Company, a branch of our business, adopted first

in 1908. That was not Large whiskey which we bought on the market. The whiskey in the purchase and sales account was bought on the market. The "Old Whiskey" account represented whiskeys that were not sold on contracts, produced new in the season of the fall and spring of any distilling season and at the end of the year, which was on June 30th every year, the distilling season was known as the fall of one year and the spring of the next. The whiskeys not sold on contract were carried over as an investment of my own. I had capital and I employed that capital that way, kept them there until I wanted to market them or sell them like any other investment. The Large Distilling Company was simply the name under which I, as an indidivual, traded and did business. There was no corporation. Either myself or the Large Distilling Com-
[fol. 95] pany would keep our old whiskey for a certain time and then sell it at the regular market price for that age whiskey. The older the whiskey the better the price it would command. It had a bonded period. It could remain in bond eight years and then it would be gotten out of bond. I would sell it at various times. I think in 1922 all the whiskey in that account was four years old or older. Whiskey could not be sold in glass until it was four years old, but it could be sold in the barrel. Most of our sales were made in glass. We preferred to sell it that way, because it carried the quality direct to the consumer, we were pretty sure, and any other way that could not be controlled. All our customers were wholesale liquor dealers. Wholesale liquor dealers were rectifiers, compounders. They used Large Whiskey as a basis of blends to some extent, but it is well known that there were a lot of other whiskey they could use for blending purposes in which the market price was so much lower than the market price of the same age of Large, and they would not throw our whiskey into the tub. They would put it out bottled in bond. Large, was not heavy-bodied as many of the others. That is why they preferred others, to some extent, for blending. Ours was a gentleman's drink.

Redirect examination:

The whiskey in the "Old Whiskey" account was sold either in bulk or in glass. If bulk it would be transferred

to the bottling department and go out in glass. We did not encourage any business in bulk because we did not know it would do any good for the brand. The good it would do for the brand was for the customer to get the flavor, and if we sold it in bulk, there might be some other name on it, but if he got it in bottles it helped to build up goodwill. Out of the "Old Whiskey" account we sold in [fol. 96] bond only to the people and gave them warehouse receipts and they turned those receipts in to us, and then for bottling, with bottling charge, or we could sell it—both after prohibition for our own account through wholesale druggists. We never sold any case goods. We would not be in competition with the wholesale liquor dealers. We had to leave that for him to distribute and have some business on our brand, or he would not keep it in stock. There is no difference between making the sales from the "Old Whiskey" account and making sales of whiskey that we distil. It is the same whiskey. One is a personal investment in "Old Whiskey" account and there is not any other except the purchase and sale, the stocks that you buy and resell to supply the customers.

We don't speak of the sale of whiskey in bulk. We speak of whiskey receipts. Bulk goods refers generally to tax-paid whiskeys in bulk, but we sold the whiskeys represented in bond, represented by warehouse receipts and they were brought into us to be transferred into glass at a cost per case for bottling.

In 1921 I found out that my conclusion reached in 1918 that you had to quit business in about four years was correct. I had to quit business as a result of the Willis-Campbell Act.

Recross-examination:

The "Old Whiskey" account was a personal investment. I had the means to carry whiskey for my own account and invest my capital in whiskey. I was running the Large Distilling Company. I ran my books to carry my personal investments in those books and that was one of them. I am the sole owner of the Large Distilling Company. I distinguish between personal investments and the business of the Large Distilling Company as follows: I invested my money in the whiskey as an investment and carried it until

[fol. 97] I would want to realize. I had and exercised that privilege in my own books, which will show that I had a number of other investments, International Banking Corporation, New York, and other investments in those books prior to 1908. Each year I put some new whiskey into the "Old Whiskey" account and took it over as a personal investment. It is a personal investment because it is a separate business. I took it over and put capital in that to keep my money employed, instead of letting it all go out and letting the other fellow make a lot of money.

In addition to the business of distilling whiskey, I was in the business of selling the product. The business of selling the finished product after it had been produced was taken care of in the purchases and sales account. I made a practice of actually selling the Old Whiskey as well as making a practice of producing whiskey. I sold the Old Whiskey through the Large Distilling Company and sold my personal investments. I did not go outside and get somebody else to sell it for me. I sold it in the departmental account of the Large Distilling Company. I certainly did call it a personal investment, because I set it up in a certain account on my books with other investment accounts in the books but which were not as close to me as whiskey.

Redirect examination:

My business as a distiller was selling whiskey on contract.

Recross-examination:

That was not our sole business. We bought and sold on purchases and sales accounts. We bottled in bond for the account of owners of whiskey in bond. We had profits in several accounts. We were not tied down exclusively to one business. I had investments in my books. I employed money. I had more capital than I needed in the business [fol. 98] to continue the distilling business, selling under contracts as we had been doing. As a matter of fact I was in other businesses besides distilling.

Grosvenor Nicholas, a witness produced by the appellant, on oath, testified in substance as follows:

I am vice-president and director of Fabor Company and Gregg of New York, cigar importers and dealers. I have been connected with that company for about two years since my business was consolidated with theirs.

We were importers of cigars and formerly importers of wines and spirits, located in New York. It was only the cigar part of our business that was consolidated with this other company.

I went into the business of importing and dealing in wines and whiskeys in 1907 and continued therein until after prohibition.

Our company dealt in rye whiskey, but principally imported wines and spirits. We were large importers of those products.

Our company bought and sold what is known as Large Whiskey. I do not recall whether we contracted for it, or how we purchased it. I knew the product of the Large Distillery well. I knew its reputation in the trade and its standing with the consumers.

Its reputation in the trade and standing with the consumers was the highest, the very best.

The immediate result of the Constitutional Amendment was that persons engaged in the whiskey business were all out of business. Certain concerns continued under a permit but the business under permit was an altogether different business from the old business before prohibition.

[fol. 99] Cross-examination:

I have tried Large Whiskey. I can't say that I ever went into the matter of the reputation of Large Whiskey with any one or that any one said anything to me concerning the quality of Large Whiskey. I was simply in the trade for many years and knew the reputation from being in the trade, just as I knew the reputation of other distillers and wine growers.

My recollection is that we carried Large Whiskey practically up until prohibition took effect, but it may be that our supply was exhausted sometime before that. We dealt with Mr. Renziehausen but I can't recollect whether we contracted in the form he testified to, that is, whether we gave him an order in advance to make so much whiskey or whether we bought some whiskey he had already made.

WILFRED S. POLLOCK, a witness produced by the appellant, on oath, testified in substance as follows:

I was formerly general manager of the liquor department or Weidemann Company, Cleveland, Ohio, and had been connected with that company since 1897. They were wholesale grocers, liquor dealers and importers since 1861. Annually, we contracted with the Large Distilling Company for as many barrels of Large Whiskey as they would permit us to buy before manufacture.

The standing of Large Whiskey in the trade was the highest because it was the whiskey that was used by the trade under the original brand. We would buy and dump many other whiskeys in the making of our blends, but the demand for Large Whiskey was such that we never did that.

We dealt to a large degree in whiskeys of many other brands, and I had occasion to acquire knowledge about many other brands.

[fol. 100] I have known Mr. Renziehausen twenty-five or thirty years and considered him one of the best distillers. I am able to express an opinion as to value of the goodwill, including trade-marks and trade brands of the Large Distilling Company. Assuming the value of the tangible assets for the years 1908 to 1912 to average $251,380.05, and the earnings to average for the years 1909 to 1913, inclusive, approximately $85,000, and considering my knowledge of the qualification of Mr. Renziehausen as a distiller, I should say that value was close to $1,000,000. I arrive at that through the ever increasing popularity of the brand under conditions existing before prohibition, and the increased distilling each year.

Cross-examination:

It is a matter of opinion whether there was any whiskey better than Large. Some people preferred Bourbon and some rye. In my opinion, ryes are the best and Large was absolutely the best rye whiskey that was made.

In arriving at the value of the goodwill, I took into consideration Mr. Renziehausen's abilities and qualifications as a distiller and other facts. I gave a good deal of weight to his ability as a distiller and to his handling of the brand of the business of the Large Distilling Company. Up to March 1, 1913, his efforts were instrumental in making the

brand valuable and they were responsible for a good deal of the value, I estimated, but not practically all of it, the quality of the goods. I did not take into consideration altogether the figures given before by Mr. Seifert. It was the increased popularity of the brand from year to year and the increased demand for it. I could not tell you how much it increased in popularity and demand each year. My value is not based entirely from those figures. Only in a measure [fol. 101] it shows a gradual increase. I did not take the figures into consideration as represented here, but I knew there was a constant increase in demand, consequently the growth in the public's favor. The figures were taken into consideration as a portion of goodwill. I do not see how I can get a value drawn from those figures. I do not just understand what you mean.

Jacob L. Crone, a witness produced by the appellant, on oath, testified in substance as follows:

I was in the wholesale liquor business from 1895 to 1919. The firm I was with bought Large Whiskey and I sold it. We dealt in all whiskeys. The selling price per gallon of Large Whiskey was always higher than other whiskeys. The maximum price for Large was $3 a gallon at one time in bond. I do not think any whiskey at that time ever reached that price.

(No cross-examination.)

George C. Howell, a witness produced by the appellant, on oath, testified in substance as follows:

I have now retired. I have been engaged in importing wines and spirits and in the wholesale liquor business in New York City since 1885 with the firm of Samuel Striter & Company, one of the largest firms in New York. I was graduated from Princeton in 1883.

I was taught to sample liquors and in about a year's time I could pick out blindfolded of twenty samples and name the distillery. I could smell and taste a sample of whiskey and name the brand. We handled Guggenheimer, Finch's

Golden Wedding, Overholt, Dillinger, Bridgeport, Vandegrift and practically every well-known brand of Mononga-
[fol. 102] hela Rye, besides a Philadelphia whiskey, Harrisville, W. Va., Mount Vernon Distilling Company.

The first time I knew of Large Whiskey was in 1890. Mr. Pontefract, of the Finch Distillery, gave me a highball of Large Whiskey. It was a beautiful whiskey. I went out to see the distillery. I have seen it quite a number of times after it was a real distillery.

We handled Large Whiskey in March, 1913. I knew about its reputation then. It had a reputation of the highest class, best reputation for bottled in bond rye of any brand in the country. That reputation continued to increase after March 1, 1913, up to the advent of National Prohibition.

I know Mr. Renziehausen's ability as a business man. He bought the formula and employed the best distiller he could get to make the whiskey. He brought that distillery, by good business methods, by advertising, by hard work, up from 3,000 barrels a year to from 8,000 to 12,000 barrels a year, nearly all of which went into glass. Mr. Striter used to say it did not make any difference how good whiskey was, the whiskey could be good, and if the man did not know how to sell it, it was no good.

It would take at least fifteen years to build up a brand of whiskey. The bottled in bond and distilling business was a stable, well-established business on March 1, 1913.

I am not a certified public accountant, and I know nothing about the legal requirements or percentage to charge up to goodwill or how to arrive at goodwill, but the amount of rye whiskey consumed in 1912 was 133,000,000 gallons and in 1913, 140,000,000 gallons, which was part blends and part bottled in bond. The bottled in bond was gradually working out the blends and getting more and more each year, because the people were getting whiskey guaranteed, not as to quality, but as to age. The ratio was probably ten
[fol. 103] of rye to a barrel of blends. There was a promotion in a year of the Dodge Brothers Company—they put their goodwill in at $70,000,000. That goodwill represented what the Dodge Brothers had done in the past in a very short time. Take the Large on the apportunity of 40,000,000 cases of whiskey a year, I should think that is the way I would figure what their goodwill might possibly be

worth. I should say it was worth at least $1,000,000. How much, I do not know. It would be more.

Cross-examination:

I am not a certified public accountant and know nothing about the legal, but taking any other business, good merchandise business, which has been promoted, United States Steel, their goodwill—you put out $100,000,000 common stock and it is worth more than preferred. What I am getting at, is goodwill in the amount of business done. The United States Steel must have had some goodwill to get its assets. It got the surplus through goodwill. I do not know anything about the manner in which goodwill is figured. I only know that as a business point of view they were unique with their method. They had taken the grand prize in so many expositions, with the quality of whiskey which was peculiarly adapted to bottled in bond, that there was no other concern in the United States had anything like the showing they had. Every other whiskey was made for blends. It was rough whiskey. The Large was a mild whiskey. They were bound to get more than their share of the business each year, increasingly. That is what I am thinking of.

I was simply a merchant but I tried to learn the business. I went through the Guggenheimer and a dozen different distilleries in this country. I have been through Scotch whiskey distilleries and gin distilleries in Holland, but never through a brandy distillery.

I value it at at least $1,000,000. I do not know how much [fol. 104] more. Considerably more than $2,000,000. I would not go higher. It would be more depending on how long you figured goodwill to last.

"If it stopped right off as this goodwill was stopped, how long are you going to figure—it shows at least that it is going to last as long as the distillery had lasted, since 1796, I should say $10,000,000 was goodwill, $10,000,000 would not be out of the way with what they had in quality and what they had in method and their slogan, 'Drink a little Large.' I saw that exhibit in the spring of 1896. Why, there was nothing like it."

I am giving you the value as of March, 1913. I have considered just what they had in the quality of their whiskey and their method, everything they had to sell, to secure the trade, to secure the business. It is true that Large Whiskey was absolutely the best bottled in bond rye whiskey made, putting it at 100 proof at four years old. The Large Whiskey was without doubt the best whiskey there was made for that purpose in rye.

I have no figures to go on in raising my value from $1,000,000 to $2,000,000. They should get a big share of that, possibly 40,000,000 cases. That was increasing.

They could get their business through the ability of the man who sells the article. John Smith may be able to get a great deal more out of something than Tom Brown is. Mr. Renzienhausen got a great deal more. He was going out for medals when the others were going to sleep.

Mr. Renziehausen would have someone trained to take his place, just the same as the President of the United States Steel Corporation. If he should die, there is another man there to take his place. If it had been run by somebody else, I wouldn't have arrived at the same figure. It is his personal ability with the quality of the whiskey that enters [fol. 105] into the value of this goodwill, which I said was $2,000,000. It is the ability to secure future business, I should say. The ability which Mr. Renziehausen had taking together with the value of the whiskey which would be kept the same and those medals were big. There were only two concerns that had them. All concerns thought they were big. The Sunnybrook Distilling Company advertised the World's Fair Prize at St. Louis. Mr. Renziehausen has got it. They considered it very valuable or they would not have advertised it.

PHILLIP W. GUNDELFINGER, a witness, produced by the appellant, on oath testified as follows:

I have been raised in the liquor business from the time I went to school and since 1899 I have been interested in it with my father, upon until 1920 when we quit on account of prohibition. We engaged in the wholesale and retail business and catered to the family trade. Our business was very similar to that carried on by Schuetz-Renziehausen & Company and we were competitors. They owned

trade-marks and trade brands of value and carried a very large stock of whiskey, liquors, gins and other kindred stocks, larger than our stock and in excess of their requirements. Both Mr. Schuetz and Mr. Renziehausen had a pretty good understanding of the wholesale liquor business, but not altogether as to my way of doing it. They catered to a good class of trade. They were in business as far back as I can remember. I do not know of any firm having a better standing in the City of Pittsburgh.

Assuming for a period of approximately five years prior to March 1, 1913, that the tangible property, and assets, the stock in trade which they would sell, approximated about $309,000, and that for the same period their net earnings [fol. 106] were approximately $27,000, I contend as a buyer that a man could readily pay $100,000 for the goodwill, trade-marks and trade brands of the Schuetz-Renziehausen & Company and work out very nicely.

Cross-examination:

I have heard the testimony of other witnesses.

I think they carried an entirely too large a stock for the profits they made. They were running a business as much for a hobby as for a business. They carried a lot of valuable stocks, valuable wines that there was not any demand for in proportion to the amount of rye whiskey there was a demand for. The average liquor dealer did not carry to my mind the number of choice liquors that they did. It did not pay. They were wealthy and did not have to care if brandy evaporated four or five gallons a year that the other fellow that had to watch his dollars would. They did not care how much evaporated out of a barrel of the old whiskey as long as they could say, "This is the oldest stuff in Pittsburgh." Their stock was well selected if you wanted to brag about the good stuff you had, but from a business standpoint they carried a larger stock than was necessary.

It was a hobby to have fine old goods. They were prouder of boasting on brandy or fine Rhine wines than selling whiskey, although they had a very prominent brand of whiskey and we bumped against it in competition.

I don't think it was necessary for them to carry $300,000 worth of merchandise to make $27,000, so if I were to buy it and pay them, say $400,000, $300,000 for their merchandise and $100,000 for goodwill, I would sell the stock and reduce it to $100,000. Then I would figure I could make 6 per cent on that $100,000 and another 6 per cent on the $100,000 of goodwill. I am accustomed to figuring 6 [fol. 107] per cent. I do not get much at five. That would be $12,000. I could make $27,000 on the stock of liquors costing me $100,000 just the same as they did on a stock worth $309,000. I would then have $15,000 a year to apply against goodwill and in six or seven years I would have the goodwill paid off figuring at $100,000.

W. O. FREY, a witness produced by appellant, testified, on oath, substantially as follows:

I live in Pittsburgh and am now engaged in the building supplies business. Prior to that and since 1893, I was a wholesale liquor dealer, in business with my father until sixteen years ago.

I knew the firm of Schuetz-Renziehausen & Company. They conducted the same kind of business I did and were in competition with me. They had a much larger business than I had. At or about March 1, 1913, they had the highest class of trade. I am able to express an opinion as to the March 1, 1913, value of the goodwill of that company.

Considering the length of time in which they had been in business, their knowledge of their own business and that they had tangible assets averaging for the five-year period prior to March 1, 1913, $309,000 and earnings over the same period of approximately $27,000, I would think the fair market value of their goodwil, trade-marks and trade names as of March 1, 1913, to be around $100,000. I would arrive at that the same as Mr. Gundelfinger. They carried too much stock, had too much money employed in the business and a big part of it would be not productive.

Cross-examination:

I place a value around $100,000. It would be guess work if I would put an exact amount on it. They were con-

sidered among the best firms in the city and they sold noth-
[fol. 108] ing but high class trade, and they also had a reputation if you wanted to get Large nobody else had it, you could get it from them, and it was the most popular brand in that district.

It is a matter of opinion whether you place it at $50,000 or $200,000. I am in the liquor business and I figured. I did not necessarily pick the values out of the air.

I carried between $50,000 and $75,000 worth of stock. Some years ago I made $10,000, others $8,000, others $15,000. I averaged for the five lean years prior to March 1, 1913, between $6,000 and $7,000. The value of my goodwill all depended on what I could get if I was going to sell. I would get all I could possibly get. I could not put a sum on it. I did not think of selling, never had it in mind and never gave it any thought or consideration. I did not know a thing about their business arrangements nor what they were actually making. In arriving at the value of $100,000 I always understood they did a big business, sold lots of goods, I had no idea what their sales were at all. They were considered to have the outlet for Large. I think because Mr. Renziehausen owned the Large Distillery. Other factors were their reputation, the length of time they were in business, the time it would take to build that up.

B. Stanley Taylor, a witness produced by the appellant, testified, on oath, substantially as follows:

I was employed by Mr. Renziehausen as a bookkeeper from 1907 to 1920. The "Old Whiskey" account was opened July 1, 1908. I opened it. Whiskey that was made on contract was during the period of distilling, called new whiskey. On June 30, it was new whiskey. On July 1, it was old whiskey. The account was opened to get the old
[fol. 109] whiskey out of the merchandise account where the production was made, merchandise account was the new whiskey produced. Practically all the whiskey produced was sold by contract but he would carry what he did not sell and that would be the old whiskey.

The "Old Whiskey" account was carried on the books of the Large Distilling Company for Mr. Renziehausen's in-

vestment, capital account. He handled all his investments in the books of the Large Distilling Company. It was carried as an investment account because he wanted to invest in Large Whiskey.

Cross-examination:

I don't know how they handled old whiskey prior to 1908.

Whatever he did not manage to sell on contracts he would keep in the hope of selling later and he would naturally have to keep on doing that at least until 1908 and possibly earlier. He had to sell it every year after 1908. He sold part of this old whiskey from time to time, every year.

J. H. Weeks, a witness produced by the appellant, testified, on oath, substantially as follows:

I have been manager and general supervisor for Mr. Renziehausen since 1900.

Material advantage was gained from the advertising expenses set forth in Petitioner's Exhibit 38, Respondent's Exhibit "C." It was derived through the withdrawals. A distiller's prosperity was gauged by the withdrawals. It was practically a gauge of his goodwill.

I considered the payments made to the purchasers on account of tax paid on excess evaporation was the best adver- [fol. 110] tising we had on our books. That was reflected to me each year when I was closing contracts.

From 1900 to 1913, I had a chance to observe the amount of time and the nature of services rendered by Mr. Renziehausen. I think he dreamt of the brand. He was talking about it when he went to bed and when he got up. It was said by his friends he was married to the brand.

(No cross-examination.)

Whereupon the witness identified various tayles and forms of advertising, exposition awards and mostly reproduced abroad. Most of this advertising was put out during my time, some of it originated ahead of my time.

(The advertising matter was then shown to the trial member of the board and withdrawn.)

CLARK HAMILTON, JR., a witness produced by the appellant, on oath, testified in substance as follows:

I live in Wheeling, West Virginia. I am associated with Mr. Renziehausen in a capacity of a little of everything, as far as I can see, office work, outside work. I have been employed since September, 1914, and am conversant with his business affairs. I have known him at least thirty years. Before my employment by Mr. Renziehausen I was employed in the wholesale liquor business in West Virginia, and as such I had occasion to come in contact with Mr. Renziehausen very often. I first became acquainted with Mr. Renziehausen eighteen or twenty years prior to 1913. I am acquainted with Mr. Renziehausen's business ability and was so acquainted for some time prior to 1913.

From what I know, what he has been doing I think $15,-[fol. 111] 000 to $18,000 a year would be very moderate value for his services per year prior to 1913.

Mr. Renziehausen alone was responsible for building up the business of the Large Distilling Company.

Cross-examination:

I do quite a lot of outside work for Mr. Renziehausen. I was a salesman for him before prohibition. Since prohibition I have done quite a lot of office work in looking after his affairs in general and the Large Distilling Company.

I arrive at a value of from $15,000 to $18,000 a year for his services from what he has to do and what he has done. I know lots of people that get more salary than that, that do not do so much work and carry the responsibility that he carried. I mean people connected with corporations, etc., that draw larger salaries. I could not just mention any particular men, but I know there are quite a number and, as a matter of fact, I do not know what their salaries are.

Redirect examination:

I am connected as a stockholder with some corporations in Wheeling who pay salaries to the officers of more than $15,000. I do not think any man ever worked as hard as Mr. Renziehausen and I would say $15,000 is a very mod-

erate salary for what he is doing. His service is worth that much money.

Recross-examination:

I do not know that I could say right off-hand who draws a salary of from $15,000 to $18,000.

Mr. Renziehausen works eight hours a day, if not longer, really seven days a week.

I am a stockholder in the Wheeling Steel Corporation, Hazel-Atlas Glass Company and the Sterling Products [fol. 112] Company. I have not looked at the books of those companies and I could not say what salaries were paid the officers.

The deposition of MICHAEL LETZELTER was produced by the appellant, wherein the witness testified, on oath, in substance as follows:

I was in the wholesale liquor business at 4614-16 Liberty Avenue, Pittsburgh, and was engaged therein for over twenty years and handled all brands of whiskeys, including Large, Schenley, Overholt, Thompson, Dillinger, Finch, Guckenheimer and Tom Moore.

Large whiskey was a favorite brand and it always sold better than any other brand of whiskey I handled.

I always received a higher price for Large than I did for other whiskeys.

Large whiskey had a good reputation for quality and was always in demand. The name itself was well-known and made the brand. I know there was a lot of imitation labels used on the market and they would put anything in the bottle and put on a "Large" label because there was a demand for it.

The value of the goodwill of the Large Distilling Company on March 1, 1913, I would say was about a million dollars.

The reason for this opinion is that you would have to spend a million dollars to advertise it the way Large was advertised. Take our medicines, look what they spend a year to advertise their patent medicines. They spend all kinds of money.

The reason for the opinion is that it would require the investment of a million dollars in advertising and the like to build up a reputation, standing and demand such as Large whiskey enjoyed on March 1, 1913.

(No cross-examination.)

[fol. 113] The deposition of JACOB P. NILL was produced by the appellant, wherein the witness testified, on oath, in substance as follows:

I was engaged in the wholesale liquor business in McKeesport, Pa., continuously from 1885 until National Prohibition.

While in that business particularly in March, 1913, Large whiskey always in my estimation brought a larger price on market compared with other whiskeys of like kind.

I first became acquainted with Schuetz, Renziehausen & Company about 1880. They were engaged in the wholesale liquor business, the same business I was in. I knew them for close to forty years. I was personally acquainted with Mr. Renziehausen and Mr. Schuetz and to some extent familiar with their business. I knew they had special brands that were in quite a demand.

I was generally familiar with trade conditions from the time I went into the wholesale liquor business until prohibition.

McKeesport is in the Pittsburgh district not far removed from the place of business of Schuetz, Renziehausen & Company and was a competitor of mine during the time I was in business.

From my knowledge of the business of the wholesale liquor dealer, from my own experience, from my knowledge of trade conditions and from my large acquaintance and competition with Schuetz, Renziehausen & Company the March 1, 1913, value of the goodwill of the said company was in my opinion $200,000.00 to $300,000.00.

The reasons for this value is my being identified with like transactions in my own small way. Schuetz, Renziehausen & Company were widely known and did twenty times as much business. I was in business by myself and

[fol. 114] they had representatives on the road. They were one of the best known wholesale liquor dealers.

Cross-examination:

Schuetz, Renziehausen & Company sold their product all over the country, I should judge their volume of sales to be over a million dollars. I only know that by observation and coming in contact with them. I didn't have access to their books or anything.

They had a large establishement on Liberty Street in Pittsburgh between Fourth and Fifth. It strikes me that it was a four-story building and they occupied the whole of it.

I never saw a balance sheet of Schuetz, Renziehausen & Company, nor had any information as to their earnings or profits.

These factors ordinarily enter into the establishment of goodwill. By goodwill I mean the value of the business over and above the actual physical assets. The whole value should earn a certain percentage. A fair return on money invested in that business would be ten per cent. The factor of profits would enter into the valuation of the goodwill.

The way I figured the matter of goodwill is the kind of trade they had.

I know nothing about the value of their plant; nothing about the value of their physical assets, their stock in trade, machinery and equipment. I don't know what profits the company made in any year.

The deposition of JOSEPH FUHRER was produced by the appellant, wherein the witness testified, on oath, in substance as follows:

I was engaged in the wholesale liquor business at Thirty-seventh and Butler Streets, Pittsburgh, from 1892 until [fol. 115] July 1, 1919 when prohibition went into effect. The house was established in 1866.

We sold the principal brands of whiskey, also private brands, blends, wines, brandies and all sorts of liquor.

The names of the various brands of whiskeys sold by me while in business were Gibson, Guckenheimer, Overholt,

Schenley, Large and Finch's Golden Wedding. These were the principal whiskeys sold but we sold practically all the other brands in a smaller way. All of the brands mentioned were manufactured in Western Pennsylvania.

I have visited and been all through the Large Distillery. I was on the Board of Directors of the Schenley, and I am familiar with their methods. I have been all through the Finch Distillery and also through the Gukenheimer plant.

I was familiar with the methods of purchasing and disposing of whiskeys by wholesale liquor dealers. I contracted for all these whiskeys and those for which I had the largest trade I made the largest contracts.

I contracted for Large whiskey prior to the time Mr. Renziehausen was the owner, years and years ago. We dealt with Henry Large, Jr., in person, before Mr. Renziehausen had any proprietorship. We specialized on Large.

I have traveled in this country and elsewhere. I have purchased Large whiskey over the bar in Cuba, in London, all through the South and even in Canada.

It was extensively sold in the East, in Boston, New York, Philadelphia, all of the large cities of the East and it was extensively sold.

The reputation for quality would be unsurpassed. It was widely known, and the quality was as uniform as any whiskey that was ever made, in my judgment.

In our business we used it as a blend. It was used on [fol. 116] account of its stretching qualities. The flavor was heavy and you could use less in blending than you could of some brands. It was used to improve the taste and qualities of other whiskeys.

These facts were generally known to everybody who was closely associated in business.

The qualities were also very well known to the consuming public. This pertains to about the ten years prior to 1913. This was the time, in my judgment, it was before the public strongly, when it became prominent before the public.

From my familiarity with the quality and reputation of Large whiskey particularly and from my knowledge of the business as a whole, I think the value of the goodwill on March 1, 1913, of the Large whiskey would be approxi-

mately a million dollars. I consider that very conservative.

The reasons or grounds for the opinion was that if I was an investor I would cheerfully pay far more than that.

I would feel that I was making an absolutely good investment.

I was familiar with the business of Schuetz, Renziehausen & Company, engaged in the same business as myself. They were located at First and Market Street-, Pittsburgh. I have positive knowledge that they have been in business thirty years at least.

Their reputation in the trade was good. They did a large business. I was in competition with their brand for twenty years.

From my knowledge of Schuetz, Renziehausen & Company and their business, derived as heretofore stated, the March 1, 1913, value of their goodwill in my opinion would be approximately $200,000.00. I based this value on that of my own business which I valued at about $50,000.00 and I know they enjoyed a larger business than I did, three [fol. 117] or four times as much, and on that assumption I think that $200,000.00 would be a fair figure for their intangibles.

Cross-examination:

"Q. What do you mean by the term goodwill, Mr. Fuhrer?

"A. Well, long establishment in business, building up a trade, is worth something.

The question of profits do not enter into that.

"Q. So that whether or not the firm made considerable profit or not, as long as the goods were well advertised and well distributed, that company had goodwill?

"A. Well, being long established in business and having the goodwill of the customers, repeated orders, and they were sitting so that their intangible was a valuable asset.

"Q. Well, I am asking does the question of profits enter into the estimation of goodwill?

"A. Well, it naturally would, because if they were conducting their business for less than a reasonable profit, I think that would affect their goodwill to that extent."

The Large Distillery manufactured about 20,000 barrels on the average and the price in those days was about 50 cents a gallon. The element of profit in the 50 cents I could not estimate. Some derive more profits than others.

I never saw the balance sheets of the Large Distilling Company, and I was never able to learn what profits they made in any year.

I do not know the value of the Large Distilling Company plant. My estimation of a value of $1,000,000.00 for goodwill is based entirely upon the reputation of the whiskey [fol. 118] and the wide area in which it was sold and the general opinion of liquor dealers.

I do not know the amount of business done by Schuetz, Renziehausen & Company but I was active on the road all this time and I based the value on the amount of trade I had and I know they quadrupled my business, I just based it on that.

I never saw a balance sheet of the company and I had no idea as to their profits.

The deposition of J. G. HERALD was produced by the appellant, wherein the witness testified, on oath, in substance as follows:

I am a resident of Youngstown, Ohio, and have resided there for twenty-eight or twenty-nine years, and in my early days and youth was employed by John Gallagher Company, wholesale liquor dealers, and from and after 1908 was secretary and treasurer of John Gallagher Company, whose business was located at Youngstown. I was in the wholesale liquor business between twenty and twenty-one years prior to the Prohibition Act.

We handled Finch's Golden Wedding, Large, Sam Thompson, Overholt, Guggenheimer, Meadville, Sunnyside and Gibson.

Large whiskey was always very popular and in great demand, and in a number of instances it commanded from 50 to 100 per cent. more than either Thompson, Golden Wedding or Meadville, or any other of the Pennsylvania ryes that cost within 2½ or 5 cents as much for manufacturing.

The facts that, first, it was a very clean, palatable whiskey that drinkers enjoyed consuming in its natural state.

It was bottled in bond, a great portion, I believe. I know [fol. 119] that is the way we sold the most of it; 85 per cent. of all the Large we contracted for we sold bottled in bond and it at times commanded a very high figure. I think there were a number of times that the distillers were sorry it was so high, because it had gotten, they thought, too high. I believe throughout this valley Large whiskey was always in strong demand. Of course, the brand was popular generally throughout the country. It had gotten a great deal of advertising through its winning prizes, or being awarded gold medals and prizes at various fairs held here and abroad; Chicago, St. Louis and San Francisco I believe it won awards at all three places.

I noticed Large whiskey sold well outside of Western Pennsylvania; at Cincinnati, Cleveland and in the Northwest at St. Paul. For instance, George Benz at St. Paul was a big concern; every traveling man would be talking about George Benz. It was an immense institution and, I understand, he was a Large user.

Its distribution was very wide; I think it covered the entire country. The brokers in the East, we have sold some of our whiskey to brokers, both East and West.

Some whiskey we contracted for and possibly had fifteen, twenty-five or thirty-five barrels of some inspection that would command as high a price on the market as we could acquire retail, and we eliminated that cost of retailing and sold it for just as much money to the broker, where some other dealer took it, that he had to have it immediately.

I was familiar with the quality and reputation of Large whiskey at all times, because we handled the brand during all of our years in business, to some extent.

In my opinion the value of the goodwill, trade-marks and trade names, etc., of the Large Distilling Company on [fol. 120] March 1, 1913, was not less than a million dollars.

The basis for this opinion was, first of all, the goods were high class goods, good material and well distributed throughout the country, largely in glass. That meant that, instead of being sold in barrels, it was sold in quarts, pints and half-pints, and they stood around on the shelves in the bars and whole establishments where very bottle was a Large ad, and the winning of these various prizes and awards throughout the country, both here and abroad, all helped to popularize it and added to its value; and then the

word "Large" itself, there was something attractive about that in connection with whiskey. The fact that it dealt with size had something to do with it, to the consumer. It was a good name for whiskey; it was very catchy. Take the foreign element throughout the Mahoning Valley, I suppose it would apply down here just as it would in our town, where it is all iron and steel, the foreigner couldn't read or write, he would hear people talking about Large whiskey and he thought maybe you got a little more of it than you did some others, and caused him to inquire about it.

* * * * * * *

It does not make any difference where the plant is located, or how much money you have got in the plant, the question is whether you have a well-known brand of whiskey. If you have, no matter who makes it or where it is made, so long as the quality and reputation stand up, you have a market for your whiskey.

Cross-examination:

I don't know whether the Large Distilling Company sold their entire output or not. The profits of 50 per cent. or a 100 per cent., or the price of a 50 per cent. or 100 per cent. that the Large whiskey sold over the other brands, that [fol. 121] profit went to the person who contracted for the whiskey. It did not go to the distiller; he had no part in that profit at all.

In determining the value of a million dollars as at March 1, 1913, I considered, first, the product itself, because it was a high-class, clean brand of whiskey that the consumer of whiskey enjoyed drinking in its natural state. You see, there were a number of brands of whiskey which the public did not know much about; made to sell to rectifiers, who blended them with other whiskeys and sold them as their own brands. Large was not that kind of whiskey. It was sold, as I say, largely in glass; easily 85 per cent. of the Large we handled we handled in glass; and, of course, that all came bearing a label with the words "Large Whiskey," and their own attractive label on it. That gave it wide advertising, advertising, as I say, instead of a barrel; a barrel produced twelve or thirteen cases and that one

barrel had thirteen ads on it and each one of those cases had twelve, twenty-four or forty-eight ads on the bottles. After it was consumed, the empty was thrown around somewhere; it still bore the "Large" label, so the brand got a lot of advertising in glass that it would not get if sold in bulk.

I know nothing about the output or quantity of output of the Large Distillery, except what their representatives would tell us from time to time.

I know nothing about the profits of the Large Distilling Company.

I know nothing about their sales except as stated by the representative of the Large Distilling Company.

I have no idea as to the physical value of the plant; I have never been in the plant.

"Q. Then if you didn't know anything about the value of the plant and the amount of profit made by the company, how could you figure the value of the goodwill?

[fol. 122] "A. Well, because of the popularity of its name—I thought I covered that—because how well advertised it was, how well known it was throughout the country. There is a number of trade names in this country that are very popular and have a lot of value back of them. I suppose Budweiser, at one time it would take a barrel of money to have bought them."

Redirect examination:

When I placed the value on the goodwill and trade name, I didn't know anything about the value of the plants; that would be subject to an appraisal. The value of the plants would be in addition to the goodwill and trade name.

Recross-examination:

The output of the distillery had a material effect on the valuation of the goodwill, providing the concern was marketing many times more merchandise.

"Q. And that of course would enter—the profits of the company would enter into consideration of the value of the goodwill, would they not?

"A. Well, some concerns do a large business and do not make as much profit as some small, successful concerns that

market their goods in a limited territory and derive a greater return.

"Q. That is just what I am talking about. Then the element of profit does enter into consideration in the valuation of the goodwill?

"A. It surely would enter into it, if they were producing on equal basis."

And I do not know what the profits of the Large Distilling Company were.

[fol. 123] The deposition of A. J. SUNSTEIN was produced by the appellant, wherein the witness testified, on oath, in substance as follows:

I have resided in Pittsburgh since I was nine years old and I am now going on sixty-five years of age.

I was engaged in the wholesale liquor business with my father since early youth, and became a partner of the firm of Sunstein & Sons in 1882, and was practically "chief cook and bottle-washer" from that time on until we went out of business in 1919, a few months before wartime prohibition.

I also operated the Sam Thompson plant, under the name of the Thompson Distilling Company, from 1899 until National Prohibition went into effect, and we attended to the withdrawals of that whiskey until we sold our interest in 1921.

Sam Thompson pure rye whiskey was among the best known pure rye whiskeys manufactured in this country.

During the period of my experience in the whiskey business, both wholesale and distilling, we had thirteen leading brands of rye whiskey in Pennsylvania and quite a number in Maryland, such as Gibson, Guckenheimer, Overholt, Schenley, Fenwick, Meadville, Dillinger, Bridgeport, Sam Thompson, Daugherty of Philadelphia and Large.

Large whiskey, from the time they rebult their distillery, progressed constantly. There was an increasing demand for it, increasing reputation. The increasing demand and reputation was prior to 1913.

I have been on the National Distillers' and Wholesale Liquor Dealers' Association, was on their executive committee since 1901. I was its chairman for a number of years.

I was president of the association from 1903 until 1905. I was president of the Distillers' and Wholesale Liquor Deal-
[fol. 124] ers' Association of Western Pennsylvania from the time of its organization until we wound it up, after prohibition.

I had a wide acquaintance with the trade, not only on account of my connection with the association but as a leading distiller and wholesale liquor dealer. I know practically the trade of the country, leading trade anyhow, personally.

I have known the Large Distilling Company ever since I was in business, because it was a distillery that was well known fifty years ago.

The first man I knew who was connected with the Large Distilling Company was Henry Large and I knew the business from the time of Henry Large down to the present time.

C. Sunstein & Sons, the firm I was connected with, contracted each year for Large whiskey for many years, that is, we contracted for goods to be made, and during that period many times we had demands in excess of our anticipations and we had to go on the market and purchase whiskey, and if my recollection is right, we always had to pay a very handsome profit on the contract price.

I was familiar with the product, its standing in the trade and its reputation among consumers on March 1, 1913.

For a proper understanding of the value of a leading brand of whiskey, it must be considered that their earnings came from three sources, and practically all of it as result of goodwill. First: You had the profit to the manufacturer; Second: The pure rye whiskeys, the well-known brands of pure rye whiskey, did not go into consumption; that is, practically did not go into consumption until after they were four years old, and consequently the distiller had an income from storage on the whiskey, depending upon the amount of whiskey in the warehouses from time to time; Third: After
[fol. 125] the "bottled in bond" law was enacted in 1889, requiring whiskey to be bottled in bonded warehouses, and the Government affixed a stamp on the outside and did not allow any whiskey to be bottled unless it was four years old and no less than 100 proof, the demand increased on this bottled in bond, and, of course, brought in a profit on bottling. That is, for a distiller like Large or ourselves, we never sold any bottled in bond, no case goods; we sold

on contract, goods to be made; and the dealers, retail and wholesale, would send in these warehouse receipts after they were four years old and have them bottled under our brands, and we would charge so much per case for bottling. The bottling always represented a profit and many years, when grains were high, we made more money on the bottling than we did on the merchandise itself, and, of course, the demand for that came purely from goodwill.

"Q. Why was goodwill such an important element in all three sources of profit that you have mentioned?

"A. Well, the greater the demand for the whiskey, the more you could manufacture, and the more whiskey you manufactured, the larger receipts you would have from storage, and then the goodwill would manifest itself in the demand for this bottled in bond. You see, the principal distillers of Pennsylvania and Maryland only sold to the jobbing trade, and they endeavored to sell on contract; that is, goods to be made; we would go out in the fall of the year, we would announce our production, our price, and in most of the years the leading distillers, when their business, when the demand, was any good, they could sell all that they were going to manufacture during the season. Say, during the spring of 1907 and 1908, they could sell all they would manufacture, and then the trade held those warehouse re- [fol. 126] ceipts until they had the demand; some of them would trade them on the market, and of course the value of the brand would manifest itself in the price it could command in relation to other brands. If there was a good demand for it when it got to the consuming age, it would command a good price."

If my recollection serves me right, I think Large whiskey commanded a very good price during 1913 and previous years.

The March 1, 1913, value of the goodwill, trade-marks, trade names and intangible property of the Large Distilling Company;—If a man wanted to buy a distillery and a brand of whiskey to build on what he had, why a man could possibly make good interest on a million dollars or more.

Under proper conditions, a man should make $150,000 a year easily on a first-class brand, if it had good demand, and the Large Whiskey was among the leading brands of

the eastern rye whiskeys and they were the best rye whiskeys manufactured in this country.

Cross-examination:

I have never seen the balance sheets of the Large Distilling Company.

I know nothing about its assets in 1913.

I have no idea as to what value the plant was carried on the books, but I think some judgment as to possible value.

When I placed the value of a million dollars on the goodwill of the company, I did not consider any of those things, and when I say that the plant ought to have made $150,000 yearly, I do not know that the plant did make that much. [fol. 127] I would consider a fair return on money, for the purpose of valuing goodwill, 10 per cent., that is, 10 per cent. net.

I think the value of the goodwill of the Large Distilling Company is worth more than the physical assets.

I think in many of the plants that had a good reputation the goodwill was worth more than the plant itself.

I have no knowledge of the accountant's method of setting up goodwill.

"Q. And you assumed the fact that they make about $150,000 a year—you base your value of the goodwill upon those profits, taking into consideration your opinion of the physical value of the plant?

"A. Well, that is increased—Take a brand like Large, there was an increasing profit constantly, year by year. There was hardly a year, commencing around 1912—1911 you might say—the demand for bottled in bond was constantly increasing; and there was also a profit I didn't mention. In buying goods on the market, buying back your own goods and holding it for a time, and then getting the market increase on that whiskey, in a good many years we made good profit in that way ourselves."

My knowledge of my own business and the profits of my own distillery shows to some extent the value placed on the goodwill of the Large Distilling Company. I think they bottled more in the latter years than we did, because they produced a larger quantity than we did.

Redirect examination:

I have no idea as to the value of the Large Physical assets, but I think a man should be able to make a fair return [fol. 128] on a million dollar investment in the goodwill and intangibles of the Large Distilling Company.

When I spoke of brand I meant the value of the goodwill. As an illustration, you take during the period of years very often you could get a rye whiskey that would probably cost a much to manufacture as another. I have in mind, say, two brands; There was a brand on the Allegheny River here, manufactured, made out of rye and malt, and used to sell at four years old, around 52½ to 55 cents; and Large would sell at the same time around 85 to 90 cents, at the same age. The one at 85 to 90 cents was in greater demand than the whiskey that was selling at 52½ to 55 cents at the same age. That was because the one was well-known, and the other had to sell commercially, on its commercial value, irrespective of brand.

Recross-examination:

Most of the rye distillers used about the same materials. They may have changed the quantities as between malt and rye, and their process may have been somewhat different, and should have no effect on the price. The only reason for the increase in price would be by reason of freight or something of that kind.

The deposition of Robert Lewin was produced by the appellant, wherein the witness testified, on oath, in substance as follows:

I have resided in the City of Pittsburgh for the past forty-four years, and prior to National Prohibition was in the wholesale liquor business in Smithfield Street, Pittsburgh.

I was engaged in this business for a period of over thirty years. During that period I handled Overholt, Finch, [fol. 129] Guckenheimer, Large, Thompson, Bridgeport, George W. Jones, Dillinger, Logansport and Gibson.

During the thirty years I was engaged in this business I was well acquainted with trade conditions and also acquainted with other dealers familiar with the market in

which these various whiskeys were sold and the parts of the country in which they were consumed.

I first began to deal in Large whiskey about 1889, at which time Henry Large was in control. Then it became Mr. Renziehausen and I continued to deal with the Large Distilling Company until prohibition came.

The concern was over a hundred years old, so far as I can remember, when I first began to deal with them.

Their whiskey was in great demand and it was a very good quality. On or about March 1, 1913, there was a great demand for Large whiskey, greater than any other demand.

It was a whiskey that enjoyed a wide distribution. The demand for that whiskey was such that we really tried to keep a customer from buying it, because we could not get enough. I had to go on the market and pay fancy prices. I bought twice as much on the market as I contracted for. The prices that we sold, we really did not care to make such big investments. For instance, I could have bought a very good brand, speaking of buying in bond, not tax paid, such as Gibson, Finch, Thompson, Overholt, for perhaps 75 to 85 cents; for Large, I had to pay as high as $2.75 per gallon.

Large whiskey commanded about 25 per cent more on the market than any other brand. We never drummed up trade for Large.

From my knowledge of trade conditions and dealings in Large whiskey, I would have been perfectly willing to take an interest in the company at an investment of a million [fol. 130] dollars or over for the goodwill, trade-marks and trade name of Large whiskey, and I would feel that I was making a good investment.

Mr. Renziehausen and the trade dealt by contract; by that I mean, in the fall Mr. Renziehausen or one of his representatives would go to the wholesale dealer and would say, "Now, you had last year a hundred barrels. Do you want the same amount this year?" And if I say, "Yes, I will take that much," or say, "If I can get 150 or 200 barrels, I would take them," I would sign a contract. The price was set, of course, and the price was one the same as the other, never varied; the man who buys 500 barrels wouldn't get it a cent cheaper than the man who buys 25 barrels; it was just the same price to the purchaser. That is the way our contracts were made. The contracts were

made out at or before the distilling season. The contracts contained the months in which we wanted our whiskey made and then we were notified when the whiskey was made and the certificates were issued. The whiskey remained in the warehouse, for which we paid a storage, and then we tax-paid them just as we wanted them, after three or four or five or six years.

Cross-examination:

I never saw the balance sheets of the Large Distilling Company.

I have visited the plant and it was a pretty good-sized one. I cannot state the amount of money invested therein.

I do not remember the output of the distillery yearly.

I do not know what the profits of the concern were in any year. When I made the statement that I would be willing to subscribe for stock in the company with a million dollars' good will, it was based upon my own experience in the [fol. 131] business, experience among the general trade and we all had the same experience with Large whiskey, by being such a demand for it that I had to go into the market and pay fancy prices in order to obtain some of their goods. This experience outside of the Pittsburgh district.

The Large Distilling Company never overproduced. It was never a drug on the market. It was a business which was well conducted. With your permission, I will give you a little idea. During the panic in 1893, we could have bought a good Pennsylvania pure rye whiskey as low as 35 cents; Large you couldn't get, everybody would hold on it, and we had to pay even during the panic a high price for Large whiskey.

The demand was not so great for other brands as for Large.

Before I would make an investment, I would inspect the books of the company and would have some knowledge of the profits each year and would know whether the concern would pay me a proper return on the money invested.

I would like to make as much upon my investment as I could, and I know that the Large business would pay pretty well. I would judge that the business would pay 25 per cent or more from what I have heard others making on their shares.

The deposition of C. W. WELTY was produced by the appellant, wherein the witness testified, on oath, in substance as follows:

Prior to prohibition I resided in Pittsburgh and moved there from Wheeling, West Virginia, in 1914. I was engaged in the wholesale liquor business from 1876 until National Prohibition, both in Wheeling and Pittsburgh. I [fol. 132] handled most all brands of Eastern ryes and Kentucky Bourbons. I dealt in Large, Daugherty, Finch, Gibson, Sherwood, Thompson and others.

I first became acquainted with Large about 1900, or prior thereto, and continued to deal in it until National Prohibition.

I dealt in Large for about twenty or twenty-five years and its quality and reputation were of the very best. There was a good demand for it. The demand was in excess of the supply.

* * * * * * *

The market value of Large whiskey was always a little higher than the other brands.

From my knowledge of the liquor business and experience therein, and knowledge of the Large Distilling Company and its product the March 1, 1913, value of its goodwill, trade-marks and trade brands would be a million dollars at least. The reason for this value is the requtation, quality of the goods and my personal experience with whiskey, ready sale of goods.

* * * * * * *

The demand was constantly increasing and the whiskey seemed to sell itself.

Cross-examination:

I have been through the plant, but do not recall the date or dates.

I have never seen a balance sheet of the company. I do not know what the physical assets were worth on March 1, 1913. I do not know what profits were made by the company. I have an idea that they sold 8,000 to 10,000 barrels a year. That amount of whiskey ought to bring one hun-

dred thousand dollars profit or it wouldn't be a good 10 per cent on a million dollars.

[fol. 133] "Q. That would be the valuation then of the goodwill. What about the physical assets? Do you think there ought not to be a return upon the physical assets as well as upon the goodwill?

"A. I don't know anything about the assets.

"Q. Then you figure the profits at about $100,000, which would be 10 per cent upon what you figure the value of the goodwill?

"A. I don't figure their profits at that. I say, any distillery making that much whiskey should make that much profit."

I estimate the profit of 10 per cent without considering the value of the plant. I mean that if they did not have any assets at all, if they had that brand, trade-mark, and they made 8,000 to 10,000 barrels a year, I think it should pay that much profit.

I figure the goodwill of the Large Distilling Company at $1,000,000—by my experience with brand and the way the public thought of it and the demand for the whiskey.

The appellee offered in evidence joint exhibit, Commissioner's Exhibit A and Petitioner's Exhibit 36, showing, among other things, that the Large Distilling Company carried upon its books as of December 31, 1917, asset accounts and depreciation reserves accrued with respect thereto as follows:

EXHIBIT

	Cost	Depreciation
Railroad Siding	$2,498.63	$1,207.64
Buildings (new)	151,413.53	14,636.63
Four Warehouses	115,413.53	10,989.97
Machinery and Equipment	97,035.72	48,517.84
Unused Equipment (new)	2,657.13	1,284.24
Buildings (old)	5,833.85	1,399.83
Delivery Equipment	182.77	176.65
Unused Equipment (old)	1,329.75	1,285.42
New Boiler House and Stack	16,316.33	155.66

[fol. 134] The foregoing condensed statement of the evidence is hereby approved, to be incorporated in the record

on the appeal of the petitioner and on the cross appeal of the Commissioner.

Smith, Shaw & McClay, Attorneys for Petitioner. W. W. Booth, of Counsel. C. M. Charest, General Counsel, Bureau of Internal Revenue.

ORDER APPROVING STATEMENT OF EVIDENCE

Approved and ordered filed July 16, 1928.

C. Rogers Arundell, Member Board of Tax Appeals.

Certificate to foregoing paper omitted in printing.

[fol. 135] BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No., 10658

FREDERICK C. RENZIEHAUSEN, Appellant,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No., 10658

COMMISSIONER OF INTERNAL REVENUE, Appellant,

v.

FREDERICK C. RENZIEHAUSEN, Respondent

JOINT PRÆCIPE FOR TRANSCRIPT—Filed July 13, 1928

To the Clerk of the United States Board of Tax Appeals:

You will please prepare a joint transcript of the record in this cause, to be filed in the office of the clerk of the United States Circuit Court of Appeals for the Third Circuit at Philadelphia, Pennsylvania, under the separate appeals heretofore perfected to said court by the taxpayer

herein and by the Commissioner of Internal Revenue, respectively, and include in said transcript copies, duly certified as correct, of the following pleadings, proceedings and papers on file, to wit:

(1) The docket entries of the proceedings before the Board.

[fol. 136] (2) Pleadings before the Board.

(3) Appellant's Request for Findings of Fact and Conclusions of Law.

(4) Findings of Fact, Opinion and Decision of the Board.

(5) Exceptions to Findings of Fact and Conclusions of Law.

(6) Affidavit of Service of Exceptions.

(7) The taxpayer's Petition for Review.

(8) The Commissioner's Petition for Review.

(9) The Statement of the Evidence as it may be finally settled, agreed upon or approved, pursuant to Equity Rule No. 75.

(10) This joint designation of record.

Said transcript to be prepared, certified and transmitted, as required by law and the rules of the United States Circuit Court of Appeals for the Third Circuit.

Smith, Shaw & McClay, Attorneys for the Taxpayer.
W. A. Seifert, W. W. Booth, of Counsel. C. M. Charest, General Counsel, Bureau of Internal Revenue.

Certificate to foregoing paper omitted in printing.

[fol. 137] Minute entry of argument and submission November 27, 1928, omitted in printing.

[fol. 138] In United States Circuit Court of Appeals for the Third Circuit, October Term, 1928

Nos. 3940 and 3941

Frederick C. Renziehausen, Petitioner,

v.

Commissioner of Internal Revenue, Respondent

Commissioner of Internal Revenue, Petitioner,

v.

Frederick C. Renziehausen, Respondent

Petitions for Review from the United States Board of Tax Appeals

Before Buffington, Woolley, and Davis, Circuit Judges

Opinion—Filed March 7, 1929

Davis, Circuit Judge:

These cases are brought here on appeal and cross appeal on petitions to review a decision of the United States Board of Tax Appeals adjudging deficiencies in the petitioner's income taxes for the years 1918 to 1922 inclusive, except 1921, for which year there was an over-assessment. The deficiency for the year 1918 was $174,159.60; for 1919, [fol. 139] $22,495.44; for 1920, $156,362.99 and for 1922, $67,745.39. The over-assessment for 1921 was $23,924.57.

Mr. Renziehausen is a resident of Pittsburgh, and during the years in question, he was the sole owner of the Large Distilling Company and a half-owner of Schuetz, Renziehausen & Company.

The business of these companies was principally that of distilling whiskey which they sold to wholesale dealers under uniform contracts. They also carried on a warehousing business. After the whiskey was distilled under these contracts, it was stored in bonded warehouses and there remained until withdrawn by the owners who held warehouse receipts for it and paid monthly storage charges therefor.

The assets of these two companies consisted of both tangible and intangible property and the taxpayer contends

that he is entitled to a deduction for the obsolescence of this property for the years in question.

The intangible property for which a deduction is claimed are trade-marks, trade brands trade names and good will.

Sections 214 of the Acts of 1918 (40 Stat. Part I, p. 1067) and 1921 (42 Stat. Part I, p. 240) provide, "That in computing net income there shall be allowed as deductions * * * (8) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence."

The first question is whether or not a deduction in income may be allowed for the obsolescence of the trade-marks, trade brands, trade names and good will.

There is no dispute as to the value of the intangible property of these companies, and the amount of the deduction, if any, to which they are entitled is not in dispute.

[fol. 140] Trade-marks, trade brands and trade names are closely related to good will and no attempt has been made to segregate or differentiate them. The Circuit Court of Appeals for the Eighth Circuit in an exhaustive opinion by Judge Kenyon in the case of Red Wing Malting Company v. Willcuts, 15 Fed. (2d) 626, held that a deduction for the obsolescence of the good will of a brewing company was not allowable on account of the passage of the National Prohibition Act because the allowance for obsolescence is limited to such property as is susceptible to exhaustion, wear and tear by use in the business and good will is not such property.

The clause, "including a reasonable allowance for obsolescence," enlarges the allowance made for exhaustion, wear and tear of property used in the business. The first allowance is made for depreciation resulting from exhaustion, wear and tear, or the use of the property in the business. The second allowance is made for depreciation resulting from obsolescence, or the disuse of the property in the business. The cause of depreciation in the one case is from use and in the other from disuse. They are antithetical. The property, however, is the same in both cases and must be such as may be, or has been, subject to exhaustion, wear and tear, and obsolescence. Is good will such property as the Congress had in mind? Does it have the attributes implicit in the language used?

Prior to the Red Wing case the Commissioner had decided both ways as to good will: that there could be an allowance for its depreciation and that there could not be. Since that case, he has uniformly disallowed it. Consequently, his action is not persuasive either way.

The able dissenting opinions of Mr. Trammel in the Manhattan Brewing Company case, 6 B. T. A. 952 and of Judge Swan in the case of the Haberle Crystal Springs Brewing Company v. Jesse W. Clarke, Collector of Internal Revenue [fol. 141] for the Twenty-first District of New York, — Fed. (2d) —, are persuasive. However, we are not convinced of the unsoundness of Judge Kenyon's reasoning in the Red Wing case and so hold that obsolescence in this subsection is limited to property which is subject to depreciation by exhaustion, wear and tear and that good will does not have such attributes and is not such property.

The taxpayer claims deductions from income for the years from 1918 to 1921 inclusive, for obsolescence of the tangible property of the Large Distilling Company. While he may have thought that the distilling business was at an end in 1918, the fact is that this property—plant, machinery, warehouses and formulæ—was used in distilling medicinal whiskey from 1918 to 1921, just as it was before that time. This use continued until the passage of the Willis-Campbell Act on November 23, 1921 and during that period, from 1918 to the passage of this Act, in which the taxpayer manufactured 16,654 barrels of whiskey, it cannot be said that this physical property was obsolete.

For many years, since 1908, the taxpayer stored whiskey which he had manufactured but did not sell. This whiskey aged and became more valuable. He sold it all in 1922. He contends that he is entitled to have the profit made on such "old Whiskey" taxed as a capital gain at the rate of 12½ per cent instead of at the usual normal and surtax rates under the provisions of section 206 (a) (6) of the Act which provides:

"The term 'capital assets' as used in this section means property acquired and held by the taxpayer for profit or investment for more than two years (whether or not connected with his trade or business), but does not include property held for the personal use or consumption of the

taxpayer or his family, or stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year."

[fol. 142] It seems to us this "old whiskey" was clearly a part of the stock in trade and would or should have been properly included in his inventory at the close of any taxable year just as any other whiskey on hand should have been.

The Board held that the Large Distilling Company became obsolescent in 1921. The Willis-Campbell Act was approved and became effective on November 23, of that year. Thereafter the Commissioner refused to issue a permit to the Company to distill medicinal whiskey and still refuses. He says that the plant, tangible property other than the bonded warehouses, did not become obsolete in 1921, or it would not have done so if a permit had been issued to the Companies to distil medicinal whiskey. As a matter of fact, however, no permit has been issued. But he says that since it is possible that a permit may be issued at some future date, the plant did not become and is not obsolete. The difficulty with this argument is that it is an assumption contrary to fact. It is entirely hypothetical. The fact is the plant became entirely obsolete on November 23, 1921, and the allowance made by the Board for depreciation on account of obsolescence, which as to amount, is not disputed, was justified by the facts in the case.

The Board found that because of the type of construction of the four warehouses of the taxpayer, they cannot be adapted or converted to any other purpose than the storage of whiskey in bulk. They have a total capacity of 55,000 barrels which did not exceed the normal needs of the business. Because of restrictions imposed by the "Food Control" Act upon the use and transportation of cereals and grains for beverage purposes, no whiskey was manufactured in 1917 from May until December 31. On January 1, 1918, there were stored in the warehouses 35,365 barrels of whiskey. The Board found that the total capacity of the [fol. 143] warehouses was needed in the petitioner's business. The Board further found that:

"The deduction for obsolescence, we believe, like those for depreciation and depletion, should be based upon actualities, as nearly as that may be possible; and this is necessary if the deduction is to be a 'reasonable' one as the statute contemplates. To require that the entire obsolescence should be spread and deducted from income as the remaining 27,393 barrels of whiskey, at the close of 1921, are withdrawn, would result in postponing the entire obsolescence deduction to years subsequent to 1921, when as a matter of fact obsolescence was sustained in that year to the extent of the reduction in the useful and valuable capacity of the warehouses. In view of the foregoing, it is our opinion that the petitioner is entitled to a deduction, for 1921, for obsolescence of the warehouses, in an amount representing the same proportion of the depreciated cost as the number of barrels representing the reduction in the useful and valuable capacity, plus the number of barrels withdrawn from November 24, to December 31, 1921, to wit: 27,607, bears to 55,000; and that for 1922 petitioner is entitled to a like deduction based upon the proportion which the number of barrels withdrawn during that year, to wit: 1,761, bears to 55,000, or in such manner that when the entire amount of whiskey has been withdrawn the entire cost of the buildings shall be returned by way of obsolescence and depreciation."

The respondent says that this conclusion is unsound for the reason that:

"If the Commissioner at the present time should issue a permit for the manufacture of medicinal whiskey, the taxpayer's warehouses could be used for the storage of that whiskey just as they were used in the taxable years. Certainly it can not be said that the taxpayer suffered a loss or obsolescence of warehouses which may subsequently be used as effectively as before the passage of the Willis-Campbell Act."

[fol. 144] This contention is purely hypothetical, is based upon possibilities and assumptions, up to this time, contrary to fact and may never in the life of the taxpayer become a fact. It is really no answer to the Board's conclusion which is hereby affirmed on this point.

A decree may be entered in accordance with the above conclusions, and costs of the respective petitions for review shall be charged against the respective petitioners.

A true Copy. Teste: —— ——, Clerk of the United States Circuit Court of Appeals for the Third Circuit.

[fol. 145] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT, OCTOBER TERM, 1928

No. 3940 (List No. 106)

F. C. RENZIEHAUSEN, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appeal from the United States Board of Tax Appeals

JUDGMENT—Filed Mar. 7, 1929

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this Court that the order or decree of the said Board of Tax Appeals in this cause be, and the same is hereby, affirmed.

Philadelphia, March 7, 1929.

J. Warren Davis, Circuit Judge.

[File endorsement omitted.]

[fol. 146] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT, OCTOBER TERM, 1928

No. 3941 (List No. 107)

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

F. C. RENZIEHAUSEN, Respondent

Appeal from the United States Board of Tax Appeals

JUDGMENT—Filed Mar. 7, 1929

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this Court that the order or decree of the said Board of Tax Appeals in this cause be, and the same is hereby, affirmed.

Philadelphia, March 7, 1929.

J. Warren Davis, Circuit Judge.

[File endorsement omitted.]

[fol. 147] Clerk's certificate to foregoing transcript omitted in printing.

[fol. 148] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

Docket No., 3940

FREDERICK C. RENZIEHAUSEN, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No., 3941

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

FREDERICK C. RENZIEHAUSEN, Respondent

STIPULATION AND ADDITION TO RECORD—Filed in Supreme Court May 27, 1929

It is hereby stipulated and agreed by the parties hereto by their respective attorneys of record:

1. That the printed Request for Findings of Fact and Conclusions of Law filed with the United States Board of Tax Appeals be considered a "Supplemental Transcript of Record" in these appeals, and the filing of twenty-five copies [fol. 149] thereof is waived.

2. That the second paragraph of page 56 of the Transcript of Record be amended to read as follows:

"Ordered and decided that there are deficiencies for the years 1918, 1919, 1920 and 1922 in the respective amounts of $174,159.60, $22,495.44, $156,382.99 and $67,745.39 and an overassessment for the year 1921 in the amount of $23,-924.57."

3. That no Supplemental Transcript of Record need be printed.

Smith, Shaw & McClay, Attorneys for Petitioner. C. M. Charest, General Counsel, Bureau of Internal Revenue, Attorney for Respondent.

Dated August 28th, 1928.

[fol. 150] Order

The foregoing Stipulation having been presented, it is hereby ordered and decreed that the printed Request for Findings of Fact and Conclusions of Law in the case of Frederick C. Renziehausen, Petitioner, vs. Commissioner of Internal Revenue, Respondent, Docket No. 10,658, be and is hereby denominated a "Supplemental Transcript of Record" of the foregoing appeals, and that page 56 of the original Transcript of Record be amended as set forth in said Stipulation, and that no Supplemental Transcript of Record need be printed.

Victor B. Woolley, C. J.

Endorsements: 3940, 3941. Stipulation for Filing Supplemental Record and Order Allowing Supplemental Record. Received & Filed Oct. 2, 1928. William P. Rowland, Clerk.

[fol. 151] Certificate to foregoing paper omitted in printing.

[fol. 152] [File endorsement omitted.]

[fol. 153] Supreme Court of the United States

Order Allowing Certiorari—Filed October 14, 1929

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is

granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 34,245. United States Circuit Court of Appeals, Third Circuit. Term No. 114. Frederick C. Renziehausen, petitioner, vs. Commissioner of Internal Revenue. Petition for writ of certiorari and exhibit thereto. Filed May 27th, 1929. File No. 34,245.

FILE COPY

FILED
MAY 27 1929
CHARLES ELMORE CROPL
CLER

IN THE

Supreme Court of the United States

OCTOBER TERM, 1928.

NO. [redacted] 114

FREDERICK C. RENZIEHAUSEN, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI AND BRIEF IN SUPPORT THEREOF.

WILLIAM A. SEIFERT,
WILLIAM WALLACE BOOTH,
Counsel for Petitioner.

747 Union Trust Building,
Pittsburgh, Pa.

SMITH BROS. CO. INC., LAW PRINTERS, 208-212 GRANT STREET, PITTSBURGH, PA.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1928.

NO. .....

FREDERICK C. RENZIEHAUSEN, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI AND BRIEF IN SUPPORT THEREOF.

Petition.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The petition of Frederick C. Renziehausen respectfully shows:

Summary Statement of the Matter Involved.

The matter involved is (a) whether, under Section 214 (a) (8) of the Revenue Acts of 1918 and 1921, petitioner is entitled, in computing his taxable net income for the years 1918, 1919, 1920, and 1921, to deductions on account of obsolescence of trade marks, trade brands, trade names and good will of his distillery and wholesale liquor businesses, both of which were proscribed by Federal legislation; (b) whether, under the same sections of the same acts, petitioner is entitled to deductions for the same years on account of obsolescence of plant and equipment of his

distillery business; (c) whether petitioner is entitled to the benefit of the capital gain provision of Section 206 of the Revenue Act of 1921; and (d) (This point is alternative to point (a)) whether, under Section 214 (a) (4) of the Revenue Act of 1918, petitioner is entitled to a deduction for the year 1919 on account of the loss of said trade marks, trade brands, trade names and good will, based on cost, which was lower than the March 1, 1913 value thereof.

Petitioner is a resident of Pittsburgh, Pennsylvania, and during the years in question was the sole owner of The Large Distilling Company and a partner in the firm of Schuetz, Renziehausen & Company (R. 34).

The Large Distilling Company distilled rye whiskey under contract with wholesale liquor dealers. It also carried on a warehousing business. After the whiskey was distilled under contract, it was stored in bonded warehouses and there remained until withdrawn by the owners who held warehouse receipts for it and paid monthly storage charges therefor (R. 34).

The firm of Schuetz, Renziehausen & Company was engaged in the wholesale liquor business in Pittsburgh (R. 34).

On July 1, 1919 petitioner was compelled to discontinue the manufacture and sale of whiskey for beverage purposes by the so-called Wartime Prohibition Act (R. 39). This law was of a temporary character but on January 16, 1920, and before the temporary restrictions had been withdrawn, the constitutional amendment prohibiting the manufacture and sale of alcoholic beverages became effective, thus permanently destroying the business of petitioner, except for medicinal purposes, and that purpose in turn, was to all effects and purposes destroyed by the passage of the Willis-Campbell Act on November 23, 1921

(R. 40). By January 31, 1918, it was reasonably apparent that the constitutional amendment would be adopted. Petitioner became convinced in 1918 that the distillery part of his business was through for all time and that the business as a whole would be entirely wound up and liquidated within four years (R. 39).

Medicinal whiskey was manufactured in 1919, 1920 and 1921 but no whiskey has been manufactured since November 23, 1921 (R. 40).

Petitioner claimed a March 1, 1913 value of $1,000,000.00 for the trade marks, trade brands, trade names and good will of The Large Distilling Company (R. 27 (5)) and a March 1, 1913 value of $115,500.00 for the similar assets of Schuetz, Renziehausen & Company (R. 27 (6)). The respondent admitted the values in his brief filed with the Circuit Court of Appeals (R. 138).

Petitioner in 1908 commenced to invest his excess funds in whiskey, distilled by The Large Distilling Company, which he carried as an investment until maturity. This was a personal investment of the petitioners but for the purpose of convenience it was carried on the books of The Large Distilling Company, petitioner having for a long period of time carried personal investments on those books (R. 44). Part of the whiskey was sold in 1922 after being carried as an investment by the petitioner for a period of more than two years (R. 44).

The Large Distilling Company is and has been since 1921 in the process of liquidation (R. 42) under certain restrictions and limitations imposed by various Federal and State prohibition laws (R. 42).

The case was tried before the Board of Tax Appeals which body adjudged deficiencies of $174,159.60, $22,495.44, $156,362.99 and $67,745.39 for the years 1918, 1919, 1920 and 1922, respectively, and an overassessment for the year 1921 in the amount of $23,924.57 (R. 56).

A petition for review was filed (R. 68) and the judgment of the Board of Tax Appeals was reviewed and affirmed by the United States Circuit Court of Appeals for the Third Circuit (R. 137-142).

Your petitioner avers that the Board of Tax Appeals erred and was sustained in error by the Circuit Court of Appeals; (1) in holding that petitioner, under Section 214 (a) (8) of the Revenue Acts of 1918 and 1921, was not entitled to deductions from his gross income for the years 1918, 1919, 1920, and 1921 on account of obsolescence of trade marks, trade brands, trade names and good will of his distillery and wholesale liquor businesses; (2) in holding that petitioner, under the same sections of the same acts, was not entitled to deductions for the same years on account of obsolescence of plant and equipment of his distillery business; and (3) in holding that petitioner was not entitled to the benefit of the capital gain provision of Section 206 of the Revenue Act of 1921.

Your petitioner further avers that the Board of Tax Appeals erred in denying petitioner's alternative contention, that, under Section 214 (a) (4) of the Revenue Act of 1918, he was entitled to a deduction from his gross income for the year 1919 on account of the loss, based on cost which was less than the March 1, 1913 value, of the trade marks, trade brands, trade names and good will of his distillery business, and that the Circuit Court of Appeals erred in failing and refusing to pass upon this question.

Reasons Relied on for the Allowance of the Writ.

1. The Circuit Court of Appeals in affirming the judgment of the Board of Tax Appeals and in refusing to permit petitioner to take deductions from gross income for the years involved on account of the obsolescence of

trade marks, trade brands, trade names and good will, has laid down a rule which is in conflict with the rule established by the Circuit Court of Appeals for the Second Circuit in *The Haberle Crystal Springs Brewing Company v. Clarke, Collector,* 30 F. 2nd 219. The Circuit Court moreover treated the Haberle decision as only a dissenting opinion.

2. The Circuit Court of Appeals has decided a doubtful question involving the construction of a taxing statute in favor of the Government and against the taxpayer contrary to the principle of law announced by this court in *Gould v. Gould,* 245 U. S. 151; *United States v. Merriam,* 263 U. S. 179; and *Bowers v. New York & Albany Lighterage Co.,* 273 U. S. 346.

3. The Circuit Court of Appeals in affirming the judgment of the Board of Tax Appeals and in holding that petitioner was not entitled to deductions from gross income on account of the obsolescence of plant and equipment of a distillery due to the assured passage of National Prohibition, has decided an important question of Federal law in a way probably untenable. The lower court assumes obsolescence to be the same as obsoleteness. The former is the state of becoming obsolete, the latter is the attainment of that state.

4. The question whether petitioner is entitled to the benefits of the capital gain provision of the Act of 1921 is one of far-reaching importance and is also one of first impression. The sale of assets in the course of liquidation amounts to no more than the realization and return of capital. It is not taxable except as the sale of a capital asset. The matter involves a determination of an important question of general law for the guidance of all taxpayers whose business is in liquidation.

5. The Circuit Court of Appeals failed to pass upon an alternative question fairly and properly presented to

it when it failed to decide whether petitioner was entitled to a deduction from gross income of the loss, based on cost which was less than the March 1, 1913 value, of the trade marks, trade brands, trade names and good will of the distillery business. This error, we respectfully submit, amounts to such a departure from the usual course of judicial proceedings as to call for the exercise of this Court's power of supervision.

6. All questions involved are of general importance. The same principles are involved in a number of cases now pending before the courts, the Board of Tax Appeals, and the Treasury Department. For the information of taxpayers generally all questions, we respectfully submit, should be authoritatively determined by this Court.

Wherefore, your petitioner prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Third Circuit, commanding that Court to certify and to send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket No. 3940 October Term, 1928, *Frederick C. Renziehausen, Petitioner, v. Commissioner of Internal Revenue, Respondent,* and that the said judgment of the United States Circuit Court of Appeals for the Third Circuit may be reversed by this Honorable Court and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just; and your petitioner will ever pray.

FREDERICK C. RENZIEHAUSEN,

By WILLIAM A. SEIFERT,

WILLIAM WALLACE BOOTH,
Counsel for Petitioner.

BRIEF IN SUPPORT OF PETITION.

I.

Opinions Below.

The opinion of the Board of Tax Appeals (R. 31) is reported at 8 B. T. A. 87. The opinion of the Circuit Court of Appeals is not yet reported but is found in the Record at pages 137-142.

II.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on March 7, 1929 (R. 142). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925, c. 229, section 1, 43 Stat. 938, and under Section 1003 (a) of the Revenue Act of 1926, c. 27, 44 Stat. 10.

III.

Statement of the Case.

A statement of the case appears in the petition and in the interest of brevity is not repeated.

IV.

Specification of Errors.

1. The Circuit Court of Appeals erred in holding and deciding that the March 1, 1913 value of the trade marks, trade brands, trade names and good will of a distillery and of a wholesale liquor business were not subject to obsolescence as a result of federal legislation which proscribed such businesses.

2. The Circuit Court of Appeals erred in holding and deciding that the depreciated value of the plant and equipment of a distillery was not subject to obsolescence as a result of federal legislation which proscribed such business.

3. The Circuit Court of Appeals erred in holding and deciding that a taxpayer, sole owner of a distillery, is not entitled to be taxed at the capital gain rate on profit derived from the sale of whiskey held by him as a personal investment for more than two years.

4. The Circuit Court of Appeals erred in holding and deciding that a taxpayer is not entitled to be taxed at the capital gain rate on profits derived from the sale of assets during the process of forced liquidation.

5. The Circuit Court of Appeals erred in failing or refusing to pass upon the question (alternative to Error 1) whether a taxpayer is entitled to deduct from his gross income as a loss the cost of the trade marks, trade brands, trade names and good will of his distillery business which was proscribed by federal legislation.

V.

Argument.

AS TO OBSOLESCENCE OF INTANGIBLES.

The decision of the Circuit Court of Appeals in the instant case is directly in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *The Haberle Crystal Springs Brewing Co. v. Clarke,* 30 F. 2nd 219.

We respectfully submit that the correct principle for the solution of this question is to be found in the decision in the *Haberle* case, *supra* and in the dissenting opinion of the Board of Tax Appeals in the *Manhattan Brewing Company* case, 6 B. T. A. 952.

Prior legislation and the construction of the Act of 1918 by the Treasury department confirm the intention of Congress to grant such deductions.

Advisory Tax Board Memorandum 44 (C. B. 1, p. 133).

Bulletin F, "Depreciation and Obsolescence".

Article 163, Regulations 45.

O. D. 472, C. B. 2, p. 141.

O. D. 298, C. B. 1, p. 138.

Law Opinion 862, C. B. 1, p. 127.

Dissenting opinion of Mr. Trammell in *Manhattan Brewing Company* case, *supra.*

Intangible assets are subject to exhaustion. The statute is silent on the nature of the assets subject to exhaustion, wear and tear, including obsolescence. The only requirement is that they be used in the business. The exhaustion, wear and tear does not have to be the result of use in the business. Wear and tear relate to physical life. Exhaustion and obsolescence relate to economic or commercial life. Intangible assets can become exhausted, destroyed and obsolete even as tangible assets.

The conflict of authority on this question shows the doubt that exists as to the intention of Congress. All doubts involving the construction of taxing statutes are to be resolved in favor of the taxpayer. A taxing statute is not to be extended beyond its clear import. There is no clear import here that Congress intended to allow a deduction for obsolescence of tangible property and not for intangible property. *Gould v. Gould,* 245 U. S. 151; *United States v. Merriam,* 263 U. S. 179; *Bowers v. New York & Albany Lighterage Co.,* 273 U. S. 346.

AS TO OBSOLESCENCE OF TANGIBLES.

The Circuit Court of Appeals held that because the plant and equipment were being used until the passage of the Willis-Campbell act they were not obsolete. The

manifest error, we submit, is in the assumption that the deduction was for obsoleteness, rather than for obsolescence. The deduction for obsolescence is valid even though the property is still being used in the business. It is allowed to compensate for a reasonably foreseen loss of useful value prior to natural life and due to economic or commercial causes.

If the decision in the instant case be permitted to stand it will in all probability mean that the Treasury Department will allow no taxpayer any deduction for obsolescence until the property has become obsolete. That deduction is provided for in another section of the act.

AS TO CAPITAL GAIN.

This question, whether stock in trade or inventory becomes a capital asset immediately upon the cessation of the usual course of business and the beginning of forced liquidation, is one of first impression. It is also one of great importance in the general law of the land. An authoritative decision is needed for the guidance of all taxpayers whose business is in liquidation.

It involves a construction of Section 206 of the Revenue Act of 1921, a beneficial provision to aid and assist those who have capital assets for sale. It was passed with the intention of relieving from the burden of the high tax brackets, those whose profit was derived from a single transaction and not from recurring transactions. A taxpayer in liquidation has no means of making a profit from recurring transactions or from a continuing business. When his assets are sold he has no further means of replenishing them and thus continuing in business for profit. Hence Congress said he shall not be required to pay the high tax. A decision to the contrary, we respectfully submit, would violate the spirit of the act and the intent of the legislative body.

AS TO LOSS OF INTANGIBLES.

This question is alternative to the first and principal question involved. Petitioner contended that if he were not entitled to deductions from gross income on account of the obsolescence of intangibles, he was entitled to a deduction in the year 1919, the year in which it was reasonably foreseen that his business would be proscribed by the ratification of the Eighteenth Amendment, on account of the loss, based on cost which was less than the March 1, 1913 value, of the trade marks, trade brands, trade names and good will of his distillery business.

The Board of Tax Appeals held, as a matter of law, that the ratification of the Eighteenth Amendment on January 16, 1919 did not destroy the business of The Large Distilling Company or render its intangibles obsolete because it continued to manufacture whiskey for medicinal purposes until November, 1921 (R. 45, 46, 47).

The question was fairly and properly presented to the Circuit Court of Appeals (R. 75) but that Court failed to pass on the question in any manner whatsoever. The failure of the lower appellate court to pass upon a question properly presented to it amounts, we most respectfully submit, to such a departure from the usual course of judicial procedure as to call for the exercise of this Court's power of supervision.

If petitioner is denied both his first point and this alternative point he is left in the anomalous position of having lost a valuable capital asset without the right to take any deduction whatsoever therefor from this gross income in the year he sustained the loss.

CONCLUSION.

Because of the far-reaching effect of the opinion below; because of its conflict with a decided case in another circuit; because of its failure to construe a doubtful statute

in favor of the taxpayer; because the Court below failed to pass upon a question properly presented to it; because of the manifest importance of an authoritative rule for the guidance of all taxpayers, who had formerly been engaged in the distilling business or whose business is in liquidation; and because the matters involved are of great importance in connection with the revenue laws and of such novelty and general interest as to merit a review of the case by this Court, it is most respectfully submitted that the petition for writ of certiorari should be granted.

Respectfully submitted,

WILLIAM A. SEIFERT,
WILLIAM WALLACE BOOTH,
Counsel for Petitioner.

APPENDIX.

Statutes Involved.

Section 214 (a) (4), Revenue Act of 1918

"(a) That in computing net income there shall be allowed as deductions (4) losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in a trade or business; * * *"

Section 214 (a) (8) Revenue Act of 1918

"(a) That in computing net income there shall be allowed as deductions: (8) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business including a reasonable allowance for obsolescence. In the case of such property acquired before March 1, 1913, this deduction shall be computed upon the basis of its fair market price or value as of March 8, 1913."

Section 206 (a) (6) Revenue Act of 1921

"(a) That for the purpose of this title: (6) The term 'capital assets' as used in this section means property acquired and held by the taxpayer for profit or investment for more than two years (whether or not connected with his trade or business), but does not include property held for personal use or consumption of the taxpayer or his family, or stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year."

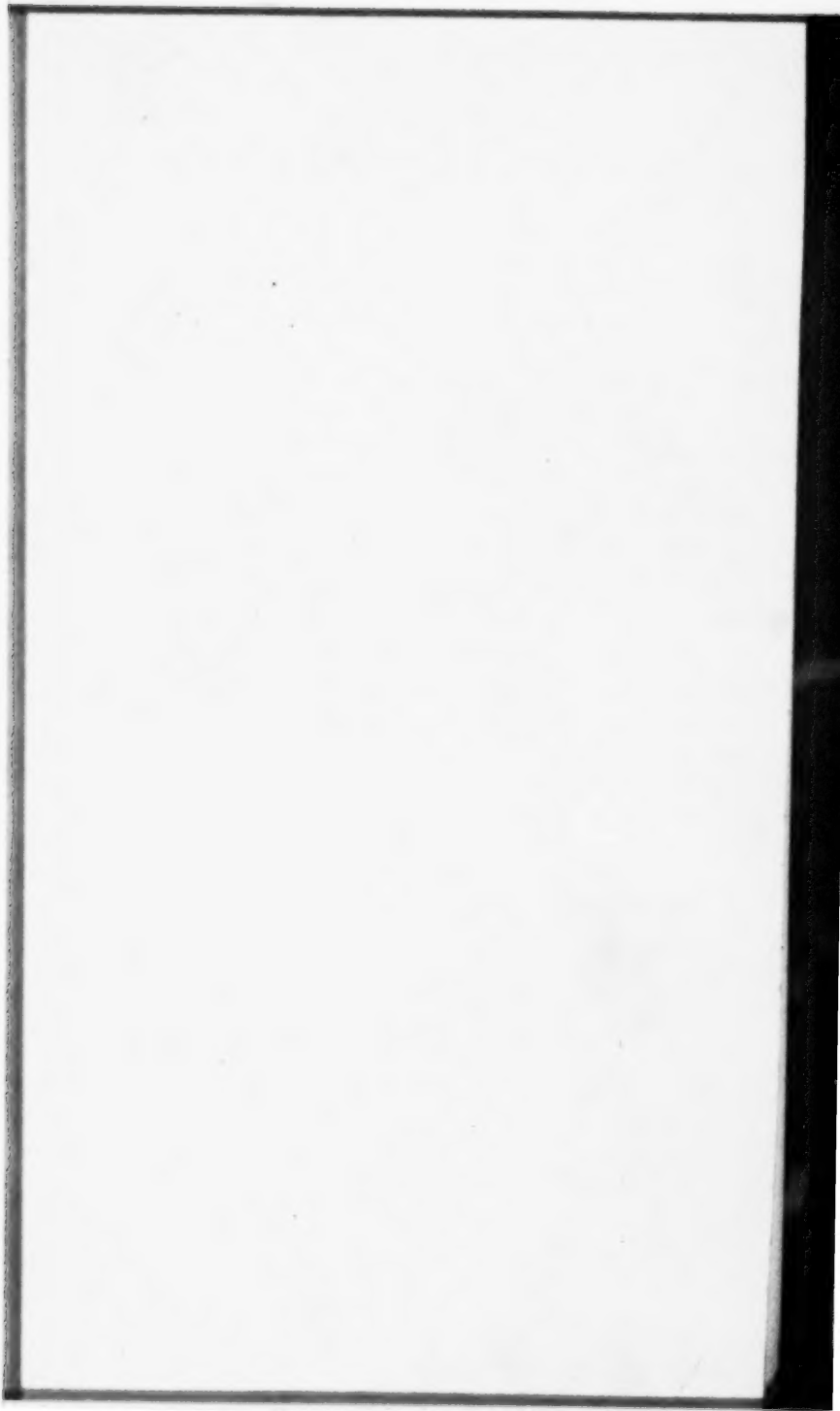
Section 206 (b) Revenue Act of 1921

"(b) In the case of any taxpayer (other than a corporation) who for any taxable year derives a capital

net gain, there shall (at the election of the taxpayer) be levied, collected and paid, in lieu of the taxes imposed by sections 210 and 211 of this title, a tax determined as follows: A partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner provided in sections 210 and 211, and the total tax shall be this amount plus 12½ per centum of the capital net gain: but if the taxpayer elects to be taxed under this section the total tax shall in no such case be less than 12½ per centum of the total net income. The total tax thus determined shall be computed, collected and paid in the same manner, at the same time and subject to the same provisions of the law, including penalties, as other taxes under this title."

Section 214 (a) (8) Revenue Act of 1921

"(a) (8) That in computing net income there shall be allowed as deductions: (8) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence. In the case of such property acquired before March 1, 1913, this deduction shall be computed upon the basis of its fair market price or value as of March 1, 1913."



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Supreme Court of the United States

OCTOBER TERM, 1929

NO. 114

FREDERICK C. RENZIEHAUSEN, Petitioner,

v.

ROBERT H. LUCAS, as Commissioner of Internal Revenue.

BRIEF FOR PETITIONER.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

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Pittsburgh, Pa.

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Supreme Court of the United States

OCTOBER TERM, 1929

NO. 114

FREDERICK C. RENZIEHAUSEN, Petitioner,

v.

ROBERT H. LUCAS, as Commissioner of Internal Revenue.

BRIEF FOR PETITIONER.

Opinions Below.

The opinion of the Board of Tax Appeals (R. 28) is reported at 8 B. T. A. 87. The opinion of the Circuit Court of Appeals for the Third Circuit (R. 113) is reported in 31 F. (2d) 675.

Jurisdiction.

The Judgment of the Circuit Court of Appeals was entered on March 7, 1929 (R. 118, 119). The petition for writ of certiorari was filed on May 27, 1929 (R. 121), and the writ was granted October 14, 1929 (R. 120).

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925, c. 229, section 1, 43 Stat. 938, and under Section 1003 (a) of the Revenue Act of 1926, c. 27, 44 Stat. 10.

Old Colony Trust Company et al., Executors, v. Commissioner of Internal Revenue, 279 U. S. 716, sustains the jurisdiction of this Court.

Statement of the Case.

Petitioner is a resident of Pittsburgh, Pennsylvania, and during the years in question was the sole owner of The Large Distilling Company and a partner in the firm of Schuetz, Renziehausen & Company (R. 31).

In 1796 Jonathan Large founded a whiskey distilling business, under the trade name of the Large Distilling Company, at Mount Washington (now a part of Pittsburgh), Pennsylvania. Three years later the distillery was moved to Jefferson Township, Allegheny County, Pennsylvania, where the business has been carried on since that time. From 1884 to 1897 the business was conducted as a partnership, composed of Henry Large and his wife, and the petitioner, Renziehausen. In 1897 Renziehausen became sole owner of the business, and thereafter to the present time conducted it as a sole proprietorship (R. 31).

The Large Distilling Company distilled rye whiskey under contract with wholesale liquor dealers. It also carried on a warehousing business. After the whiskey was distilled under contract, it was stored in bonded warehouses and there remained until withdrawn by the owners who held warehouse receipts for it and paid monthly storage charges therefor (R. 31).

"Large" whiskey, by which name the product of the Large Distilling Company was generally known, was distributed by wholesale and retail liquor dealers throughout the whole of the United States. It was generally regarded by the wholesale trade as one of the leading rye whiskeys of the country. For a long period

prior to 1913 and thereafter until the Large Distilling Company ceased distilling for beverage purposes in 1917, there was a steady growth in the demand for "Large" whiskey. The company seldom operated its distillery to full capacity. It was the practice to determine upon the quantity of whiskey to be distilled in the following season before soliciting contracts from the wholesale trade, and contracts were accepted with due regard to the total quantity to be distilled. Usually the quantity specified in the contract of a particular wholesale dealer was based upon the quantity upon which that dealer was making tax payments. The purpose of this was to prevent as far as practicable, speculation in warehouse receipts for "Large" whiskey. Because of these business practices, the demand for "Large" whiskey, as a general rule, exceeded the supply (R. 33).

From 1899 to 1913, inclusive, the Large Distilling Company expended for advertising the total sum of $82,500.02; and from 1914 to 1921, inclusive, it expended for the same purpose the total sum of $86,155.61. The advertising consisted of installing exhibits at local and international expositions, well-designed show cards, and displays in leading trade journals, newspapers, theatre programs, whiskey blotters, and the distribution of price lists. It exhibited its product at ten international expositions, viz: Chicago, 1893; Paris, 1900; St. Louis, 1904; Liege, 1905; Milan, 1906; Jamestown, 1907; Brussels, 1910; Ghent, 1913; London, 1914; and San Francisco, 1915; at nine of which it was awarded the grand prizes (R. 33).

In addition to the amounts expended specifically for advertising, the Large Distilling Company, between 1899 and 1913, inclusive, paid to its customers the total sum of $55,781.10 for leakage; and from 1914 to 1921, inclusive, the sum of $13,300.14. Leakage refers to the

evaporation while the whiskey is stored in the Government bonded warehouses in excess of the Government allowance, and upon which the owners of the whiskey were required to pay the tax. The tax on excess evaporation was paid by the owners and they were reimbursed by the Large Distilling Company, although there was no specific provision in the contracts under which the company could be held liable (R. 33, 34).

On July 19, 1897, the Large Distilling Company purchased a trade-mark for $5,000 cash (R. 34).

At March 1, 1913, the Large Distilling Company owned trade marks, trade names and trade brands as follows: Five-pointed star within a star; the label "Large Whiskey"; the slogan "Drink a Little Large"; and the company also had registered the label "Large, Established 1796, Monongahela Pure Rye Whiskey"; and "Pure Monongahela Rye Whiskey Made by Henry Large, Jr., Pittsburgh, Pennsylvania" within a circle (R. 34).

From the time he became a partner in the Large Distilling Company in 1884 to and including 1912 the petitioner Renziehausen was not paid any salary for his personal services. A reasonable compensation for the period 1908 to 1912, inclusive, for the services he rendered to the business would have been $15,000 per annum (R. 35).

The firm of Schuetz, Renziehausen & Company was engaged in the wholesale liquor business in Pittsburgh, selling brandies, cordials, fine liquors, and wines. At March 1, 1913, and thereafter until January 16, 1920, the effective date of the Eighteenth Amendment, the firm enjoyed the patronage of the most substantial retailers in the territory in which it did business (R. 38).

At March 1, 1913, Schuetz, Renziehausen & Company owned registered trade-marks for "Fort Pitt

Whiskey", "Diamond Monogram Whiskey", and "Crusador Dry Gin" (R. 38).

Liquidation of the business of Schuetz, Renziehausen & Company was begun in 1920 and completed in 1925. When prohibition legislation became effective its stock of merchandise consisted of brandies, cordials, gins, other fine liquors, and wines. The wholesale and retail drug trade would not buy this class of merchandise. A permit was obtained from the Commissioner of Internal Revenue to donate the stock to hospitals in accordance with their authorized quota, but this method of liquidation took too long and in 1925 all of the remaining stock was dumped in the sewers of the building, under Government supervision (R. 38).

The last whiskey produced by the Large Distilling Company for beverage purposes was distilled in May, 1917. Thereafter and until January 16, 1920, the effective date of the Eighteenth Amendment, no whiskey could be produced for beverage purposes because of war-time prohibition. With the imposition of war-time prohibition and the progress which had been made toward adoption of the Eighteenth Amendment, petitioner became convinced in 1918 that the distilling part of the business of the Large Distilling Company was through for all time, and that the business as a whole would be entirely wound up and liquidated within four years. During 1919 petitioner became aware that he could lawfully manufacture whiskey for medicinal purposes; and in the fall of that year the Large Distilling Company resumed distilling operations for the production of whiskey for medicinal purposes and continued such operations until at or about November 23, 1921, when, because of the enactment of the so-called Willis-Campbell Act, which provided that whiskey could be manufactured for medicinal purposes only under permits issued by the Commissioner of Internal Revenue,

and petitioner having failed to secure such a permit, distilling operations ceased (R. 35).

Petitioner claimed a March 1, 1913, value of $1,000,000.00 for the trade marks, trade brands, trade names and good will of The Large Distilling Company (R. 10, 23 (19)) and a March 1, 1913, value of $115,500.00 for the similar assets of Schuetz, Renziehausen & Company (R. 23 (23)). The respondent admitted the values in his brief filed with the Circuit Court of Appeals and the Circuit Court found there was no dispute as to the value of the intangible properties nor to the amount of the deduction, if any, to which petitioner is entitled (R. 114).

The depreciated value of the physical properties of The Large Distilling Company on January 1, 1918, was $276,652.79. The salvage value was $19,375.00 (R. 36, 37).

NOTE: There is a transposition in the findings of the Board. The total cost on January 1, 1918, should be $392,681.24 instead of $329,681.24. A correction for such error would give petitioner a larger deduction than he claims due to an undisclosed error in the itemized figures. Petitioner, however, only claims the deduction on the correct figures shown above.

The Eighteenth Amendment to the Constitution of the United States was proposed to the several legislatures of the States for ratification by Joint Resolution of Congress, which Resolution was deposited in the Department of State on December 19, 1917 (40 Stat. Pt. 1, p. 1050). It was ratified January 16, 1919, and became effective January 16, 1920.

Petitioner in 1908 commenced to invest his excess funds in whiskey, distilled by The Large Distilling Company, which he carried as an investment until maturity. This was a personal investment of the petitioner's but for the purpose of convenience it was carried on the books of The Large Distilling Company in an account captioned "Old Whiskey", petitioner having for a long period of time carried personal invest-

ments on those books (R. 39). Part of the whiskey was sold in 1922 after being carried as an investment by the petitioner for a period of more than two years (R. 39).

The Large Distilling Company is and has been since 1921 in the process of liquidation (R. 37) under certain restrictions and limitations imposed by various Federal and State prohibition laws (R. 37).

Petitioner claimed (a) deductions from gross income for income tax purposes on account of obsolescence of intangible property of both his distillery and wholesale liquor businesses (R. 4, 5, 27, 30), which businesses were proscribed by Federal legislation; (b) deductions on account of obsolescence of tangible property, plant and equipment, and in the alternative, deductions for depreciation sustained and a deduction for loss of useful value of tangible properties in 1921; (c) that Section 206 of the Revenue Act of 1921 (R. 5, 30), providing for the computation of tax on capital gain, was applicable to the disposal of whiskey after the advent of National Prohibition on two theories; first that the whiskey had been held by him as a personal investment for more than two years (R. 5, 47), and second that the sale of assets during the process of forced liquidation amounted to the sale of capital assets and not to the sale of inventory (R. 48). Petitioner also claimed, as an alternative to the claim for obsolescence of intangibles, that he was entitled to deduct the loss, under Section 214 (a) (4) of the Revenue Act of 1918, based on cost, of the intangibles of the distillery business which was proscribed by Federal legislation (R. 30, 40).

The Commissioner of Internal Revenue disallowed all of these claims (R. 14-16). The Board of Tax Appeals allowed deductions for depreciation sustained in

the years 1918, 1919, 1920 and 1921 and for obsoleteness or loss of useful value of tangible properties, plant and equipment, except bonded warehouses, which it found occurred in 1921, but decided in favor of the Commissioner as to the other questions involved (R. 28-48). The Circuit Court of Appeals affirmed the decision of the Board (R. 113-118), and from that decision the petitioner applied for a writ of certiorari, which writ was granted on October 14, 1929 (R. 120).

Specification of Errors.

1. The Circuit Court of Appeals erred in holding and deciding that the March 1, 1913, value of the trade marks, trade brands, trade names and good will of a distillery and of a wholesale liquor business were not subject to obsolescence as a result of Federal legislation which proscribed such business.

2. The Circuit Court of Appeals erred in holding and deciding that the depreciated value of the plant and equipment of a distillery was not subject to obsolescence as a result of Federal legislation which proscribed such business.

3. The Circuit Court of Appeals erred in holding and deciding that a taxpayer, sole owner of a distillery, is not entitled to be taxed at the capital gain rate on profit derived from the sale of whiskey held by him as a personal investment for more than two years.

4. The Circuit Court of Appeals erred in holding and deciding that a taxpayer is not entitled to be taxed at the capital gain rate on profits derived from the sale of assets during the process of forced liquidation.

5. The Circuit Court of Appeals erred in failing or refusing to pass upon the question (alternative to

Error 1) whether a taxpayer is entitled to deduct from his gross income as a loss, the cost of the trade marks, trade brands, trade names and good will of his distillery business which was proscribed by federal legislation.

Summary of Argument.

The Revenue Act of 1918, Section 214 (a) (8) enlarges the deduction on account of exhaustion, wear and tear of property used in business by including therein a reasonable allowance for obsolescence. The deduction is additional or supplemental to the usual deduction for depreciation.

The word "property" includes intangibles such as good will. Good will is subject to exhaustion and to obsolescence. Exhaustion and obsolescence relate to economic or commercial life. Wear and tear relate to physical life. The exhaustion and obsolescence do not have to be the result of use in business. The only requirement is that they *be used* in the business. The word "including" is a word of enlargement equivalent to the word "also" and to the conjunction "and", thus creating a new and distinct deduction.

The construction of the Revenue Act of 1918 and subsequent Acts by the Treasury Department confirms the intention of Congress to grant a deduction for obsolescence of good will.

The depreciated value of the plant and equipment of a distillery is subject to obsolescence as the result of prohibiting Federal legislation even though the plant was used for the manufacture of medicinal whiskey during the course of the passage of such legislation, but not after November 23, 1921. It was foreseen in 1918 that there would be an end to the distilling business for

all purposes within a four year period. The deduction is allowed to compensate for a reasonably foreseen loss of useful value prior to natural life and due to economic, commercial or extraordinary causes.

The capital gain provision was passed with the intention of relieving from the burden of the high tax bracket those whose profit was derived from the sale of capital assets held for more than two years. Petitioner's business was that of manufacturing whiskey on contract. He personally held manufactured whiskey for over two years as an investment which was not part of the stock in trade of his distillery business. Such whiskey was, therefore, a capital asset.

Immediately upon the cessation of the usual course of business and the beginning of involuntary liquidation, such whiskey became a frozen capital asset. The term "stock in trade" necessarily means that of a going concern or business. A taxpayer in liquidation has no means of making a profit from recurring transactions or from a continuing business. When his assets are sold he has no further means of replenishing them and thus continuing in business for profit.

If it be held that the intangibles are not subject to obsolescence then a deduction should be permitted on account of the loss thereof occasioned by prohibiting Federal legislation. The loss should be based on cost. When a going business is lost or destroyed its good will is lost or destroyed. The distillery business was destroyed by Federal legislation.

Argument.

I.

INTANGIBLE ASSETS CONSISTING OF TRADE MARKS, TRADE BRANDS, TRADE NAMES AND GOOD WILL OF A DISTILLERY AND OF A WHOLESALE LIQUOR BUSINESS ARE SUBJECT TO OBSOLESCENCE DURING THE YEARS 1918, 1919, 1920 AND 1921 UNDER THE APPLICABLE REVENUE ACTS AS A RESULT OF FEDERAL LEGISLATION WHICH PROSCRIBED SUCH BUSINESSES.

The Revenue Act of 1918 (40 Stat. Part I, p. 1067) Section 214 (a) (8) provided that in computing net income there should be allowed as deductions to individuals

> "a reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence;"

A. The Nature of the Deduction.

The reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, as contemplated by the statute, regardless of whether it is referred to as depreciation or as something else, is that amount which should be set aside for the taxable year in accordance with a consistent plan by which the aggregate of such amounts for the useful life of the property in the business will suffice, with the salvage value, at the end of such useful life, to provide in place of the property its cost, or its value as of March 1, 1913, if acquired by the taxpayer before that date. It excludes any idea of a mere reduction in market value or loss not resulting from normal wear and tear or exhaustion based upon the estimated life of the asset.

The theory of a depreciation allowance is to provide for the restoration of capital over the period of its useful life. Thus, it being the purpose of the statute to allow a restoration of capital over the period of its useful life, it is at once apparent that in certain unusual cases the allowance for depreciation would be inadequate to effect such restoration of the cost or the March 1, 1913 value of an asset. Such unusual cases are those where assets are gradually supplanted and rendered obsolete by new inventions, by changes in style, etc. In such cases when it becomes certain that the assets will, as a result of external factors, within a certain length of time become obsolete or useless, the usual deduction for depreciation will not suffice to return the capital invested or the March 1, 1913 value at the end of the shortened period. To meet this situation Congress supplemented the allowance for "exhaustion, wear and tear of property used in the trade or business" by "including a reasonable allowance for obsolescence".

The Circuit Court of Appeals in the instant case held that

> "The clause, 'including a reasonable allowance for obsolescence,' enlarges the allowance made for exhaustion, wear and tear of property used in the business. The first allowance is made for depreciation resulting from exhaustion, wear and tear, or the use of the property in the business. The second allowance is made for depreciation resulting from obsolescence, or the disuse of the property in the business. The cause of depreciation in the one case is from use and in the other from disuse. They are antithetical. The property, however, is the same in both cases and must be such as may be, or has been, subject to exhaustion, wear and tear,

and obsolescence. Is good will such property as the Congress had in mind? Does it have the attributes implicit in the language used?" (R. 114).

We respectfully submit that obsolescence is not the result of disuse but is the result of lapse of time, changes in the art, prohibition legislation, etc. Property may be in the state of becoming obsolete and still be used in the business. The deduction should be allowed when the life of the asset has a definite termination due to external factors not necessarily the result of use in the business even as a deduction for depreciation is allowed while the property is still in use.

The Circuit Court of Appeals for the Eighth Circuit in the case of *Red Wing Malting Co. v. Willcuts,* 15 Fed. (2d) 626, in commenting upon this section held:

> "It would seem quite apparent, therefore, that Congress was not intending to add a new and independent deduction. It was merely trying to provide the restoration of capital value of a depreciable asset over the period of its useful life by allowing something, known as obsolescence, as an additional element to exhaustion, wear, and tear. This legislative history sustains, we think, the conclusion to which we are forced that the phrase 'including a reasonable allowance for obsolescence' is one of specification and enlargement; that it is closely connected with and relates to the subject-matter of the other phrase of said subsection (7), and applies only to such property therein designated used in the business as is subject to exhaustion, wear, and tear."

Petitioner contends that obsolescence is an element of exhaustion and that intangible assets are as much

subject to exhaustion as are tangible assets, and further that the exhaustion including obsolescence need not be caused by use in the business, but that the deduction is allowed if the assets, subject to exhaustion and obsolescence, are used in the business.

The determination of the question therefore depends upon the question whether good will is property which is subject to exhaustion and obsolescence.

B. Good Will is Property Within the Purview of Section 214 (a) (8) of the Revenue Act of 1918.

The word "property" as used in the Act is not used in any restricted sense. *Lynch v. Alworth-Stephens Company,* 267 U. S. 364. The Act does not specify any particular property. Therefore, all kinds of property, real, personal and mixed, tangible and intangible, must be held to be included in the term.

Good will has been best defined by Mr. Trammell in his dissenting opinion in *Appeal of Manhattan Brewing Co.,* 6 B. T. A. 952, as follows:

> " 'Good will' has been defined as being the advantage or benefit which is acquired by an establishment beyond the mere value of capital stock, funds or property employed therein in consequence of the general public patronage and encouragement which it receives from the constant or habitual customers on account of its local position, or from celebrity or reputation for skill or affluence or punctuality, or from other accidental circumstances or necessities or even from ancient partialities or prejudices. *Brown v. Benzinger,* 118 Md. 29, 84 Atl. 79; *Haugen v. Sundseth,* 106 Minn. 129,

118 N. W. 666; *Goetz v. Ries,* 123 N. Y. S. 433; *Johnson Co. v. Roberts,* 159 N. Y. 70, 53 N. E. 685; *Morgan v. Perhamus,* 36 O. S. 517; *Storey on Partnership,* Sec. 99".

Good will is property in and of itself. It is intangible in nature. It is something that may be the subject of ownership, may be transferred, and may be protected by law. The term "property" includes good will. The importance of good will property has been universally recognized. *28 Corpus Juris,* 730; *Metropolitan Bank v. St. Louis Dispatch Co.,* 149 U. S. 436; *Coca Cola Bottling Co. v. Coca Cola Company,* 269 Fed. 796; *Washburn v. National Wall Paper Co.,* 81 Fed. 17.

Good will, however, has no existence except in connection with a going business and it may be bought and sold in connection with a going business as an incident or element thereof. *Camden v. Stuart,* 144 U. S. 104; *Sawilowsky v. Brown,* 288 Fed. 533.

Trade marks, trade brands and trade names are likewise property of an intangible nature. They cannot be separated from good will as it is impossible to allocate the value of the intangibles. They are in fact a part of and included in good will.

C. Good Will Is Property Which Is Subject to Exhaustion and to Obsolescence. The Deduction Is Not Limited to Assets Which Are Subject to Wear and Tear by Use in the Business.

"Obsolescence is defined in *Webster's New International Dictionary* as 'state of becoming obsolete' and obsolete is defined as 'no longer in use'; 'neglected'. Obsolescence can be distinguished from

'wear and tear' in that wear and tear refers to the physical condition, while obsolescence refers to disuse and disappearing value arising from some extrinsic or external causes, such as progress in an art, change of style, or legislation. Machinery may be in good physical condition, but, by reason of change of style or progress in the art in which it is employed, be obsolete or in a state of obsolescence. It should be noted that obsolescence is defined as the state of becoming obsolete, and does not necessarily imply that the disuse should be completed." *Manhattan Brewing Company,* 6 B. T. A. 952:

"Exhaust" is defined in the *Century Dictionary*:

"To use up or consume completely; expend or make away with the whole of; cause the total removal or loss of."

The word "exhaustion" is used in the Act in contradistinction to "wear and tear". Exhaustion results not from use but from external factors. Wear and tear from use. Certain assets become exhausted by the mere efflux of time. Leases, contracts, patents, and franchises are of this class, and deductions on account of the exhaustion, including a reasonable allowance for obsolescence of such assets, have been uniformly allowed. *Van Kannel Revolving Door Co. v. Commissioner,* 11 B. T. A. 1209; *Kentucky Tobacco Products Co. v. Lucas,* 5 Fed. (2d) 723 (D. C. W. D. Ky.); *Lassen Lumber & Box Co. v. Blair,* 27 Fed. (2d) 17 (C. C. A. 9th C.); *Lynch v. Alworth-Stephens Company, supra; Henrici Co. v. Reinecke,* 3 Fed. (2d) 34; *Kaufmann-Strauss Co. v. Lucas,* 12 Fed. (2d) 774. Articles 163 and 167 of Regulations 45, 62, 65, and 69 and Articles 203 and 207 of Regulations 74 issued under

the Revenue Acts of 1918, 1921, 1924, 1926 and 1928, respectively. T. D. 3760, IV. 2, C. B. 154.

While it may be said as a general rule that good will cannot be sold and has no existence separate and apart from a going business, it is recognized as an asset. Frequently it is the most valuable and the greatest income producing factor. Such was the situation in the instant case. The reputation of Large whiskey was of the very best. It was of excellent quality. Its sale was restricted to wholesale liquor dealers. It had won the first prize at numerous world fairs (R. 33).

Good will is a separate element forming part of the property and assets of an enterprise. It is capable of a separate valuation and may be protected by law. It may be entered separately on the books. It increases the total value of the business, but does not increase the value of the tangible assets segregated from the business. It is not indissolubly connected with specific tangible property. *Washburn v. National Wall Paper Company, supra.* Its value is not dependent upon the value of other assets. It is recognized as a separate element for the purpose of invested capital in the Revenue Act of 1917, Act of October 3, 1917, ch. 63, Sec. 207 (a), 40 Stat. 300; in the Revenue Act of 1918, Act of February 24, 1919, ch. 18, Sec. 325 (a) and Sec. 326 (a) (4) (5), 40 Stat. 1057; and in the Revenue Act of 1921, Act of November 23, 1921, c. 136, 42 Stat. 227. (see appendix).

Franchises like good will are intangible property. This court has held that payment under condemnation proceedings must be made for the destruction of a franchise to collect tolls for use of a dam and lock.

Monongahela Navigation Co. v. United States, 148 U. S. 312.

Let us assume a parallel case. Suppose that Congress had passed an Act appropriating the lock and dam of the Monongahela Navigation Company for public use, or suppose the State of Pennsylvania had passed an Act appropriating a privately owned bridge for public use, in each case to become effective two years thereafter, thus determining a definite life for the respective franchises. Upon the passage of the Acts it would be known that the franchises would be destroyed at the end of two years and the value thereof lost. How can it be logically argued that these franchises are not during those two years in a state of obsolescence? The obsolescence, however, is caused by the passage of legislation, an external factor, and not by use in the business. Neither can it be logically argued that the franchises are not used in the businesses. The earnings are not predicated upon the physical property alone. Without the franchises to collect tolls from what source would income flow? The use of good will in either a distillery or a wholesale liquor business is analogous. In the distillery business the tangible property produces the product. The good will sells it. In the wholesale liquor business the tangible property represents the place and the product. The good will is the reputation of both and the underlying cause of the sales from which the income flows. In both cases both the tangible and intangible assets are property used in the business to produce income.

Therefore, good will, like any other asset, can be destroyed if the business is destroyed. It can become obsolete if the business becomes obsolete. It can be the subject of obsolescence if the business is in the process or state of going out of use or becoming obsolete. Un-

der ordinary circumstances the life of such intangibles is indefinite and indeterminable. But ordinary circumstances are not present in this case. The passage of the Eighteenth Amendment by Congress created a most extraordinary circumstance. It was then reasonably expected, in fact it was a foregone conclusion, that the Amendment would be ratified, and it was reasonably expected that the distillery business and the wholesale liquor business would soon be matters of history, and that the value of the good will of such businesses would, within a short time, be destroyed.

While good will may not be subject to exhaustion, wear and tear including obsolescence by use in a trade or business the statute, however, does not require that the exhaustion, wear and tear, including obsolescence must be the result of use in the trade or business, but only requires that such assets *be used* in the trade or business in order to come within the provision.

The Revenue Act of 1913 provided for a deduction on account of the depreciation of property by use, wear and tear. The Revenue Act of 1916 provided for a deduction for the exhaustion, wear and tear of property "arising out of its use or employment in the business or trade." It is indeed significant that the Revenue Act of 1918 passed after Congress had had an opportunity to observe the workings of the prior Acts and the administration thereof by the Treasury Department, omitted the words "arising out of its use or employment in the business or trade".

In *Kentucky Tobacco Products Co. v. Lucas*, 5 Fed. (2d), 723, the Court held

> "Congress certainly knew that there are many species of property, such as the contract in this

case, copyrights and patents, which are used in connection with the business which produces the income taxed, and which depreciate in value as the end of their life approaches, and yet which lose none of their value as the result of their use or employment in the business. It is a fair deduction to conclude that the difference in the corresponding sections of the acts of 1916 and 1918, heretofore referred to, arose out of the desire of Congress to put such contracts and property rights upon the same footing as is given by the act of 1916 to property which is exhausted by reason of its use in the business. Whatever may have been the purpose of Congress, however, it remains that there is a very substantial difference between the corresponding provisions of the two acts, and the court is convinced that the act of 1918 authorizes a *reasonable deduction from gross income to cover exhaustion of property used in the business, whether that exhaustion is caused by the use itself or from other causes,* * * *"

Why should good will not be subject to the same exhaustion and obsolescence as patents, leases, etc.? It is not the use in the business which creates obsolescence. It is usually the development of the art in that particular industry. The invention of new apparatus, the changing trend of the times, or the passage of prohibiting legislation. The obsolescence of electrical equipment is a shining example. Ladies' clothing, particularly hats, dresses, and coats, does not become obsolete by use but by change in styles. The old "snub nose" Franklin automobile is now obsolete not because of use but because of the change in body styles. Likewise the old model "T" Ford.

The test is that the property, whether tangible or intangible, must be used in the trade or business to distinguish it from property not so used, and, if the property is used in the trade or business, the deduction for obsolescence should be allowed, no matter what causes the obsolescence or upon what kind of property it operates.

If the deduction on account of the obsolescence of property is held to be allowable only in cases where it is becoming obsolete by or on account of its use in the trade or business, the effect would be to eliminate the deduction from the statute because intangible property does not become obsolete by or as the result of use. Obsolescence is different from exhaustion, wear and tear in that it is the shortening of the useful life of an asset on account of economic conditions, new inventions, prohibiting legislation, and other causes which have no connection with the physical use of the asset. Obsolescence relates to economic or commercial life rather than physical life. Certain assets become exhausted by the mere efflux of time. Leases, contracts, patents, and franchises are of this class and deductions on account of the exhaustion of such assets are permitted by the statute and by the decisions. *Such assets become exhausted not by the use to which they are put but because they have a definite life.* The amount of use does not effect the amount of the exhaustion which takes place.

We submit the deductions should be allowed with respect to all assets used in the business when it is shown that they are approaching the end of their useful life as a result of either exhaustion or wear and tear, and if the element of obsolescence is present the deduction should also include it so that by the time the

assets are abandoned or lost the capital value will have been returned out of earnings.

If the statute be carried to its logical conclusion, an asset having an indefinite life when acquired but which thereafter becomes limited and definite by Federal legislation is as much subject to obsolescence as an intangible asset having a definite life when acquired, such as patents, contracts, leases, etc., deductions for which have been uniformly allowed.

In so far as the wholesale liquor business of this taxpayer was concerned, he was absolutely forced to give up and abandon an established business in which these intangible assets were used and were income-producing factors.

In so far as the distillery business of this taxpayer was concerned, the passage of the Eighteenth Amendment by Congress on December 18, 1917, and the ratification thereof by three States, two of which were considered doubtful, by January 31, 1918, created a universal belief that the manufacture of whiskey would soon be absolutely prohibited. This belief was borne out by the passage of the Willis-Campbell Act on November 23, 1921. In the meantime and during the years over which the obsolescence should be spread, whiskey could be manufactured for medicinal purposes but a definite life of the distillery properties had been ascertained.

Furthermore the effect of the passage of the Eighteenth Amendment completely revolutionized the petitioner's distillery business and absolutely destroyed the good will. Whiskey was no longer a beverage. The former clientele of the petitioner were forced out of business. There was no longer an open market for

their product. All sales of whiskey thereafter were made under the supervision and restriction of the United States Government. The good will which petitioner had built up and which existed as a part of his distillery business for beverage whiskey did not exist as a part of the medicinal whiskey business. An entirely different and foreign good will had to be built up in that new business. The customers were different. The market was an entirely new market inexperienced and unqualified to judge good whiskey. After prohibition it was not the quality of the whiskey which counted with the customer nor even the quantity, but only the ability to purchase and any kind of whiskey answered the purpose. The only requirement was that it should be stimulating. The new trade did not know a blended whiskey from a straight or a Rye from a Bourbon.

See:

Dissenting opinion of Mr. Trammell in

Appeal of Manhattan Brewing Co., supra.
Haberle Crystal Springs Brewing Co. v. Clarke,
30 Fed. (2d), 219 (C. C. A. 2d C., now before this Court on Writ of Certiorari.)

As we have hereinbefore argued, the intangibles in both the petitioner's distillery and wholesale liquor businesses were used in the businesses. A large part of the success of both businesses was predicated upon the use of the intangibles. The intangibles in the wholesale liquor business were absolutely destroyed when the Eighteenth Amendment became a law, and that destruction was reasonably foreseen by January 31, 1918. As to the distillery business, the destruction became absolute upon passage of the Willis-Campbell Act on No-

vember 23, 1921, and was likewise reasonably foreseen by January 31, 1918.

D. THE WORD "INCLUDING" IS A WORD OF ENLARGEMENT, HAVING THE SAME MEANING AS "ALSO" AND AS THE CONJUNCTION "AND".

The Revenue Act of 1918 was enacted in the light of the Revenue Acts of 1909, 1913 and 1916, and in respect of the deductions allowed therein was molded closely after those Acts; adding as it were new subjects as deductions as knowledge increased as to the effect of the application of the Acts to different branches of business. By way of illustration reference is made to the Revenue Act of 1909, Section 38, Par. 2nd, which provides that

> "all losses actually sustained within the year and not compensated by insurance or otherwise, including a reasonable allowance for depreciation of property, if any, * * *"

are deductible, and to the Revenue Act of 1913, which contains this provision:

> "all losses actually sustained within the year and not compensated by insurance or otherwise, including a reasonable allowance for depreciation by use, wear and tear of property, if any * * *"

and to the Revenue Act of 1916, Part II, Sec. 12, Second, which provides:

> "all losses actually sustained and charged off within the year and not compensated by insurance or otherwise, including a reasonable allowance for the exhaustion, wear and tear of property arising out of its use or employment in the business or trade; (a) in the case of oil and gas wells a reasonable allowance for actual reduction in flow and

production to be ascertained not by the flush flow, but by the settled production or regular flow; (b) in the case of mines a reasonable allowance for depletion thereof not to exceed the market value in the mine of the production thereof which has been mined and sold during the year for which the rate and computation are made, such reasonable allowance to be made in the case of both (a) and (b) under rules and regulations to be prescribed by the Secretary of the Treasury."

The present participle "including" is used in the same manner in the Act of 1918. It would be pedantic to argue that the word "including" as used in the Acts of 1909, 1913 and 1916 did not introduce a new kind of deduction different from that referred to in the words which immediately preceded it.

In the foregoing Revenue Acts a deduction for depreciation or exhaustion, wear and tear, was included in the deduction allowed for losses. In the Revenue Act of 1918, however, the deduction was disassociated from the loss provision and was given an entirely separate classification.

In Sections 214 (a) (1) and 234 (a) (1) of the Revenue Act of 1918 the present participle "including" and the words "and including" are used to introduce new subjects in addition to those which immediately precede them.

The present participle "including" has been used in many tariff acts, to-wit:

Tariff Act of July 24, 1897, c. 11, Sec. 2, 30 Stat. 197, Par. 545,

"diamonds and other precious stones, * * * including miners', glaziers' and engravers' diamonds * * *"

Tariff Act of July 24, 1897, c. 11, Sec. 2, 30 Stat. 197, Par. 339,

"embroideries and all trimmings, including braids, edgings, * * *"

Tariff Act of July 24, 1897, c. 11, Sec. 2, 30 Stat. 197, Par. 699,

"logs and round unmanufactured timber, including pulp woods, fire wood, * * *"

The word has always been construed as being the equivalent of "also". *Sullivan Machinery Co. v. United States,* 168 Fed. 561; *Hiller v. United States,* 106 Fed. 73; *United States v. Pierce,* 147 Fed. 199.

The Bureau of Internal Revenue has consistently construed the word "including" to have the same meaning as the conjunction "and".

Regulations 33, Article 147 as to losses.
Regulations 33, Article 159 as to depreciation.
Regulations 45, Article 161 as to depreciation.

This is well illustrated by the following quotation from two of the above cited regulations:

Regulations 33, Article 159:

"Section 12, Item 'Second', authorizes corporations to deduct from the gross amount of their income received within the year all losses actually sustained and charged off within the year, including a reasonable allowance for the exhaustion, wear and tear of property arising out of its use or employment in the business or trade.

"Depreciation as here used must be differentiated from the depletion, obsolescence, and other losses elsewhere provided for in these regulations."

Regulations 45, Article 161:

"A reasonable allowance for the exhaustion, wear and tear and obsolescence of property used in the trade or business may be deducted from gross income. For convenience such an allowance will usually be referred to as depreciation, excluding from the term any idea of a mere reduction in market value not resulting from exhaustion, wear and tear or obsolescence."

Regulations 74 promulgated under the Revenue Act of 1928 provides in Article 206 that the deduction for obsolescence shall be in addition to the deduction for depreciation as follows:

"Obsolescence.—With respect to physical property the whole or any portion of which is clearly shown by the taxpayer as being affected by economic conditions that will result in its being abandoned at a future date prior to the end of its normal useful life, so that depreciation deductions alone are insufficient to return the cost (or other basis) at the end of its economic term of usefulness, a reasonable deduction for obsolescence, *in addition to depreciation,* may be allowed in accordance with the facts obtaining with respect to each item of property concerning which a claim for obsolescence is made. No deduction for obsolescence will be permitted merely because, in the opinion of a taxpayer, the property may become obsolete at some later date. This allowance will be confined to such portion of the property on which obsolescence is definitely shown to be sustained and can not be held applicable to an entire property unless all portions thereof are affected by the conditions to which obsolescence is found to be due." (Italics ours).

If, therefore, the word "including" is a word of addition a different deduction is authorized for obsolescence not dependent to any extent on exhaustion, wear and tear, and as we have previously shown, goodwill is subject to obsolescence even as other assets, whether tangible or intangible.

E. THE CONSTRUCTION OF THE REVENUE ACT OF 1918 BY THE TREASURY DEPARTMENT CONFIRMS THE INTENTION OF CONGRESS TO GRANT A DEDUCTION ON ACCOUNT OF OBSOLESCENCE OF INTANGIBLES, AND SUCH CONSTRUCTION HAS THE FORCE AND EFFECT OF LAW.

The Bureau of Internal Revenue, by and including the several agencies thereof whose duty it was to administer the Revenue Act of 1918, has construed Section 214 (a) (8) of that Act to permit deductions on account of obsolescence of intangibles.

In Law Opinion 862, Cum. Bul. No. 1, page 127 (1919), the office of the Solicitor of Internal Revenue held that a deduction was permitted for the obsolescence of a wine vineyard rendered obsolete by prohibition legislation, said obsolescence to be distributed over the period elapsing between the passage of the prohibition measure and the date when abandonment occurred.

In T. B. R. 44, Cum. Bul. No. 1, page 133 (1919), the Advisory Tax Board recommended that distillers and dealers in liquor be allowed to deduct a reasonable allowance for obsolescence of good will, trade marks, or trade brands, the value of which was impaired or destroyed by prohibition legislation. Upon the strength of this recommendation Regulations 45 were revised by the Treasury Department. (T. D. 2929, Cum. Bul. 1, page 133, 1919).

In O. D. 298, Cum. Bul. No. 1, page 138 (1919), the Rules and Regulations Section of the Bureau of Internal Revenue held that deductions on account of obsolescence of intangibles allowed distillers and dealers in liquor were also applicable to brewers.

In O. D. 472, Cum. Bul. No. 2, page 141 (1920), the same section held that obsolescence of good will would be allowed in the case of the discontinuance of a going business because of the exhaustion of its source of supply, provided the good will would not be valuable in another business after the termination of the business in which the taxpayer was engaged.

Bulletin F, "Depreciation and Obsolescence", issued by the Treasury Department on August 31, 1920, contains information relative to the obsolescence of intangible assets of brewers, distillers and dealers in liquor and permits the deduction on account of obsolescence of intangibles including good will if the intangibles were in fact destroyed or became obsolete.

In O. D. 818, Cum. Bul. No. 4, page 178, the Rules and Regulations Section held

> "In the case of liquor dealers the useful life of whose intangibles, such as good will, trade marks and trade brands, was definitely limited as the result of prohibition legislation an allowance for obsolescence is permissible."

We have been unable to find any regulations or published ruling or decision of the Commissioner under the Revenue Act of 1918 on the question of the obsolescence of intangible assets which is contrary to the above opinions and rulings. There are rulings and opinions of the Commissioner, however, to the effect that when the taxpayer, instead of abandoning his business on the

effective date of prohibition legislation, continues in some other business in which the Commissioner considered that the good will continued and was not destroyed, no allowance should be made on account of the obsolescence of such good will; in other words, the Treasury Department has challenged the application of the rule but never the rule itself.

The Regulations also provided for a deduction on account of depreciation of intangibles. Article 161 of Regulations 45 provides:

> "A reasonable allowance for the exhaustion, wear and tear and obsolescence of property used in the trade or business may be deducted from gross income. For convenience such an allowance will usually be referred to as depreciation, excluding from the term any idea of a mere reduction in market value not resulting from exhaustion, wear and tear or obsolescence."

Article 163 of Regulations 45 provides:

> "Depreciation of intangible property.—Intangibles, the use of which in the trade or business is definitely limited in duration, may be the subject of a depreciation allowance. Examples are patents and copyrights, licenses, and franchises. Intangibles, the use of which in the business or trade is not so limited, will not usually be a proper subject of such an allowance. If, however, an intangible asset acquired through capital outlay is known from experience to be of value in the business for only a limited period, the length of which can be estimated from experience with reasonable certainty, such intangible asset may be the subject of a depreciation allowance, provided the facts are

fully shown in the return or prior thereto to the satisfaction of the Commissioner."

The latter Article when originally issued contained the following provision:

"There can be no such allowance in respect of good will, trade names, trademarks, trade brands, secret formulæ, or processes."

In 1919 after T. B. R. 44, *supra,* was published the Regulations were revised and the above clause stricken out. (T. D. 2929, Cum. Bulletin 1, page 133.) The Regulations were approved by the Secretary of the Treasury. Article 163 thereafter stood unchanged until after the decision of the Circuit Court in the case of *Red Wing Malting Co. v. Willcuts,* 15 Fed. (2d) 626, when T. D. 3980 was issued on February 23, 1927, holding that no deduction could be taken for obsolescence of good will. While they were in full force and effect the Revenue Acts of 1921, 1924 and 1926 were passed containing provisions corresponding to those of the 1918 Act and enacted without the slightest change in phraseology. The Revenue Act of 1926 was passed soon after the decision of the District Court in the Willcuts case had been handed down and it is plausible to assume that the framers of the Act did not have in mind that decision or that that decision had not been called to their attention.

The Regulations, Treasury Decisions, and Rulings hereinbefore quoted are entitled to very great respect. *Edwards v. Darby,* 12 Wheat. 206 (1827). They are not to be disregarded without the most cogent and persuasive reasons. *Robertson v. Downing,* 127 U. S. 607, 613. And when Congress in subsequent Acts makes no change in the phraseology of the section construed, the

construction of the Treasury Department must be presumed to have been adopted by Congress and to have the force and effect of law. *New Haven Railroad v. Commerce Commission,* 200 U. S. 361, 401; *Copper Queen v. Arizona Board,* 206 U. S. 474, 479; *United States v. Boston & Maine Railroad,* 279 U. S. 732.

F. As to the Spread of Obsolescence.

Your Petitioner respectfully submits that under the facts in the instant case the spread of the deduction on account of obsolescence of the intangibles of the distillery, if this Honorable Court finds that he is entitled to such deductions, should be over the period from January 31, 1918, to November 23, 1921, and the spread of the deduction on account of obsolescence of the intangibles of the wholesale liquor business should be over the period from January 31, 1918, to January 16, 1920.

The Eighteenth Amendment was proposed by Congress on December 18, 1917. By January 31, 1918, it had been ratified by three States, Massachusetts, Maryland and Kentucky, the first two of which were considered doubtful States, by a decisive vote (T. B. R. 44, *supra*), and it was then reasonably foreseen that it would be passed and that these businesses would be destroyed.

The wholesale liquor business was absolutely destroyed on January 16, 1920, when the Amendment became effective. The rulings of the Department hereinbefore referred to, support this contention.

The facts as to the termination of the distillery business are somewhat different. Medicinal whiskey was permitted to be manufactured until November 23,

1921, and on that day the business of distilling whiskey came to an absolute end. The end had been foreseen by the general public and by this petitioner in particular (R. 35). We have contended that these intangibles would have no value for the distillation of medicinal whiskey yet we submit that the termination of the spread of the obsolescence should be November 23, 1921.

The Treasury Department in the rulings hereinbefore cited and relied upon held that the period for the spread of obsolescence in such cases (both distillers and wholesale liquor dealers) should be from January 31, 1918 to the date of actual discontinuance of the business, in any event not later than January 16, 1920, the date when the Eighteenth Amendment became a law. The spread as to the distillery business should therefore either be from January 31, 1918, to November 23, 1921, or from January 31, 1918, to January 16, 1920.

The respondent in the Circuit Court of Appeals did not argue either in his brief or in his oral argument that the deduction for obsolescence should not be allowed in the years claimed by the petitioner, and the Circuit Court of Appeals held that there was no dispute as to the amount of the deduction, if any, to which the petitioner was entitled (R. 114).

II.

THE DEPRECIATED VALUE OF THE PLANT AND EQUIPMENT OF A DISTILLERY IS SUBJECT TO OBSOLESCENCE SPREAD OVER THE PERIOD FROM 1918 TO 1921, INCLUSIVE, AS A RESULT OF FEDERAL LEGISLATION WHICH PROSCRIBED SUCH BUSINESS.

The Board allowed petitioner a deduction in 1921 on account of the loss of useful value or obsoleteness of the depreciated value of all plant and equipment except bonded warehouses, and allowed a deduction in 1921 and 1922 for depreciation including obsolescence of the bonded warehouses based on the number of barrels withdrawn (R. 45). The Circuit Court affirmed the Board. The Board of Tax Appeals and the Circuit Court, however, held that because the plant and equipment were being used in the manufacture of medicinal whiskey until the passage of the Willis-Campbell Act they were not obsolete.

The manifest error, we submit, is in the assumption that the deduction was for obsoleteness rather than for obsolescence. A deduction for obsolescence is valid even though the property is still being used in the business. It is allowed to compensate for a reasonably foreseen loss of useful value prior to natural life and due to economic or commercial causes.

As the evidence shows there was no use of the distillery or any part thereof except the warehouses after November 23, 1921, and there is no doubt in our minds that the said warehouses during the years 1918, 1919, 1920 and 1921 were in the process of becoming obsolete. The prohibition amendment put them into a position of disuse. On January 1, 1922, the four warehouses, which had a total capacity of 55,000 barrels, contained only 27,393 barrels. Not a wheel was turned after November 23, 1921.

After the passage of the Eighteenth Amendment the public at large foresaw the complete downfall of the liquor business and so the passage of the Willis-Campbell Act was not an unforeseen event. It was to be expected in the natural course of events that such an Act would be passed in order to make the Eighteenth Amendment effective and in view of the activities of the prohibition element in Congress. It was not only the distiller that foresaw the elimination of the distilling business, but it was also well known to the general public that the distilling business would be prohibited within a period of about four years. Consequently obsolescence commenced on the physical properties of the distilling business in the year 1918, and ended in the year 1921. In the meantime, and during the years over which the obsolescence should be spread, whiskey could be manufactured for medicinal purposes but a definite life of the distillery properties had been ascertained, and it was almost certain that the manufacture of whiskey would be prohibited within the near future. The conclusion which the petitioner reached in 1918 that the whiskey business would be prohibited within four years was borne out by subsequent events.

A taxpayer is entitled to a deduction on account of obsolescence of tangible properties. *American Valve Company,* 4 B. T. A. 1204; *Manhattan Brewing Company,* 6 B. T. A. 952; the Opinion of the Circuit Court in the instant case, 31 Fed. (2d) 675 (R. 116).

The question as to the spread of the obsolescence is the same in respect to tangible properties as to intangible properties, and is argued under Point I, F *supra.*

III.

PROFITS DERIVED FROM THE SALE OF "OLD WHISKEY" SHOULD BE TAXED AT THE CAPITAL GAIN RATE.

The theory of the petitioner in regard to this point is first, that the whiskey had been held by him as a personal investment for more than two years, and was not part of his stock in trade, and, second, that the sale of assets during the process of forced liquidation amounts to the sale of capital assets and not to the sale of inventory or stock in trade.

A. THE "OLD WHISKEY" WAS A PERSONAL INVESTMENT OF THE PETITIONER, HELD BY HIM FOR MORE THAN TWO YEARS, AND WAS NOT PROPERLY PART OF HIS STOCK IN TRADE.

Section 206 (a) (6) of the Revenue Act of 1921 provides:

> "The term 'capital assets' as used in this section means property acquired and held by the taxpayer for profit or investment for more than two years (whether or not connected with his trade or business), but does not include property held for the personal use or consumption of the taxpayer or his family, or stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year."

Section 206 (b) provides that the taxpayer shall, at his election, in a case where he derives a capital net gain, be taxed at the rate of 12½% thereof.

The petitioner's business before prohibition was that of distilling and selling whiskey on contract at or before the time it was manufactured (R. 31). His

business was not that of manufacturing whiskey to be held in bond for future sale.

On November 23, 1921, the petitioner stopped the manufacture of medicinal whiskey and began the liquidation of his business.

The "Old Whiskey" account represented whiskey which was transferred from the distilling business to a personal investment account of the petitioner, who had been in the habit of carrying his personal investment accounts on the books of The Large Distilling Company for years. The whiskey sold from this account in 1922 had been carried for at least four or five years.

The stock in trade of the Large Distilling Company consisted of grain, rye and barley malt, empty whiskey barrels, cooperage supplies, supplies for the bottling house, material of that kind and everything else required by a distillery to manufacture whiskey. Automobiles were carried in the books of account (R. 74).

It was not the business of The Large Distilling Company to manufacture, age, and hold the manufactured whiskey in bond for subsequent sale. There is a line of demarcation between first, the manufacture of whiskey on contract and the sale thereof before it is actually manufactured, and, second, the manufacture of whiskey not on contract, the aging and holding of the same in bond for future sale. In the second instance the manufactured whiskey is stock in trade or inventory of the distiller.

In two somewhat analogous situations the Treasury Department has given the taxpayer the benefit of the capital gain rate.

In I. T. 2297, Cum. Bul. V-2, page 109, it was held:

> "However, if a (real estate) dealer can establish that any of the property sold by him was held primarily for investment rather than for sale, the provisions of Section 206 (b) of the Revenue Act of 1921 and Section 208 (b) of the Revenue Act of 1924 will apply to the taxation of the profits realized from the sale thereof."

In I. T. 2502 Internal Revenue Bulletin, Vol. VIII, 42-4389, page 3, it was held:

> "The net gain resulting from the sale of shares of stock held for more than two years by a dealer in securities may be treated as capital net gain subject to tax under section 101 of the Revenue Act of 1928, provided the stock was held by such dealer primarily for investment and was not a part of the securities traded in."

B. ALL STOCK IN TRADE OR INVENTORY BECAME A CAPITAL ASSET IMMEDIATELY UPON THE CESSATION OF THE USUAL COURSE OF BUSINESS AND THE BEGINNING OF INVOLUNTARY LIQUIDATION.

This is an involuntary and not a voluntary liquidation. It was forced upon petitioner by the Eighteenth Amendment and National Prohibition Legislation, and especially by the Willis-Campbell Act of November 23, 1921. The distillery business of the petitioner has been in liquidation since 1921 (R. 37).

Before prohibition, one who bought and sold whiskey could lawfully buy or sell from or to anyone in the open market. After prohibition, the purchase or sale of whiskey could only be made by one having a permit to sell, to one having a permit to buy.

When the petitioner, in 1922, sold his "Old Whiskey", he was selling capital assets in liquidation. It was not intended, as shown by the Act as well as the reports of the various committees in Congress at the time of the passage of the Revenue Act of 1921, that the taxpayer should be subject to a normal and surtax on income realized from the sale of capital assets. Of course, it was intended that the stock in trade of a going concern should be subject to normal and surtax rates, but it certainly was not intended that capital assets should be subject to other than the capital gain rates, if the taxpayer elected to be taxed on that basis.

A company cannot have a stock in trade if it is in the process of liquidation. The term "stock in trade" means the merchandise of a going concern or business. This petitioner was not operating a going concern and has not been since November 23, 1921. Therefore, he cannot have a stock in trade. The minute a business ceases to operate, its stock in trade becomes a *frozen asset* and the profit on the sale of such assets, if held for a period of two or more years, comes squarely within the provisions of Section 206. The fact that this distiller was forced into liquidation by the Prohibition Acts, thereby *freezing* his assets so that it was no longer possible for him either to manufacture his product or stock in trade or to sell it to the public, must be given consideration.

The distiller is forced to liquidate slowly. He cannot sell his assets direct to the public. He must await the pleasure of the Prohibition Unit in the approval of all permits, etc., necessary to sell such assets. The distiller's former customers have also been forced out of business. The sales made since January 16, 1920, are to permittees of the Government, who prior thereto did no business whatsoever with the distiller.

It has been contended that the distiller entered into a new business since January 16, 1920, *i. e.*, that of selling to the permittees. This is contrary to the facts. The distiller has not entered into a new business. He is liquidating his assets through the channels prescribed by the Government which, of necessity, must be slow, due to the restrictions and regulations governing such sales.

If the contention that the distiller is in a new business since November 23, 1921, is correct, why is it that he can no longer distill his product? What is his new business? If it be a merchandising business, how can he purchase or distill his whiskey? It cannot be done. Therefore he must be in the process of liquidation. This is the only answer to the question. A merchandising business consists of purchase and sales. A manufacturing business consists of manufacture and sales. A brokerage business consists of purchase and sales on commission. It matters not what type of business you may consider, there are two parts to the business: that of purchase and that of sale, or manufacture and sale, as the case may be. After November 23, 1921 the distiller had only one of these parts, that of sale, and even that was restricted, and there was no replacement of the goods sold and therefore no stock in trade.

If not entitled to the benefit of the capital gain provision, the petitioner is left in the absurd position of carrying on a business without having a source of supply with which to replenish his stock in trade.

We have made a careful and thorough search of the decisions but we have been unable to find any reported cases holding either for or against our contention. This question must, then, be decided upon the

law as developed by the application of common sense to the facts of the case, for law is, in its inception, only the application of common sense to the particular facts. If there be any doubt it must be resolved in favor of the taxpayer.

This question, whether stock in trade or inventory becomes a capital asset immediately upon the cessation of the usual course of business and the beginning of forced liquidation, is one of first impression.

It involves a construction of Section 206 of the Revenue Act of 1921, a beneficial provision to aid and assist those who have capital assets for sale. It was passed with the intention of relieving from the burden of the high tax brackets, those whose profit was derived from the sale of capital assets or from a single transaction and not from recurring transactions, or a continuing business. A taxpayer in liquidation has no means of making a profit from recurring transactions or from a continuing business. When his assets are sold he has no further means of replenishing them and thus continuing in business for profit. Hence Congress said he shall not be required to pay the high tax. A decision to the contrary, we respectfully submit, would violate the spirit of the act and the intent of the legislative body.

IV.

IF INTANGIBLE ASSETS ARE NOT SUBJECT TO OBSOLESCENCE, A DEDUCTION ON ACCOUNT OF THE LOSS OF SAID INTANGIBLES, BASED ON COST, AS A RESULT OF PROHIBITING FEDERAL LEGISLATION SHOULD BE ALLOWED.

This question is alternative to the first and principal question involved. Petitioner contended that if he were not entitled to deductions from gross income on account of obsolescence of intangibles, he was entitled to a deduction in the year 1919 on account of the loss, based on cost which was less than the March 1, 1913, value of the intangible assets of his distillery business.

Petitioner claims this deduction under Section 214 (a) (4) of the Revenue Act of 1918, which provided:

> "(a) that in computing net income there shall be allowed as deuctions: (4) losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in trade or business;"

The Large Distilling Company as hereinbefore set forth was engaged in the business of distilling Rye whiskey under contract with wholesale liquor dealers, and during the years prior to 1919 had secured a large and valuable clientele both among the consumers and wholesale and retail liquor dealers. This clientele used Rye whiskey as a beverage and all the efforts of the petitioner were bent towards making Large Whiskey a recognized beverage. The petitioner expended through advertising, services, etc., $578,281.12 for this purpose. While the Board made no finding of fact that such was the actual cost, although requested to do so by petitioner (R. 25 (33, 34, 35)), it did find as a fact that the expenditures for advertising and leakage had been

made, that the petitioner drew no salary, and that his services were worth $15,000.00 per year (R. 33, 34, 35). This expenditure constituted a capital asset and was completely lost on the 16th day of January, 1919, when the Eighteenth Amendment was ratified. Thereupon whiskey became a medicine and not a beverage. The clientele of the petitioner was forced out of business. The good will of both his distillery and wholesale liquor business was lost. The intangibles of The Large Distilling Company, which had been built up since 1796, were absolutely lost. The good will of a distillery manufacturing whiskey for beverage purposes would be of no value to a distillery manufacturing whiskey for medicinal purposes.

In *Jack's v. Commissioner,* 18 B. T. A. .... (not yet reported) decided December 6, 1929, the Board of Tax Appeals held that the good will of a downtown New York restaurant had been "destroyed as a result of the adoption of the prohibition amendment."

The respondent has admitted in his brief (pages 5, 28) filed in *Clarke v. The Haberle Crystal Springs Brewing Co.,* No. 68 October Term, 1929, that a deduction under this section for the loss of the property is allowable in the year in which it becomes obsolete.

The testimony supports the petitioner's contention as to the cost of the intangibles (R. 85, 87, 91, 92).

The Board of Tax Appeals held as a matter of law that the ratification of the Eighteenth Amendment on January 16, 1919, did not destroy the business of The

Large Distilling Company, or render its intangibles obsolete because it continued to manufacture whiskey for medicinal purposes until November, 1921. The Board failed to specially find as a fact the cost of the intangible assets although requested so to do by petitioner (R. 25).

The question was fairly and properly presented to the Circuit Court of Appeals (R. 58, 64), but that court failed to pass on the question in any manner whatsoever.

If petitioner is denied both his first point and this alternative point he is left in the anomalous position of having lost a valuable capital asset without the right to take any deduction whatsoever therefor from his gross income in the year he sustained the loss.

V.

PRINCIPLES OF CONSTRUCTION APPLICABLE.

The plain, obvious, and rational meaning of a statute is always to be preferred. *Lynch v. Alworth-Stephens Company,* 267 U. S. 364, *supra.* This principle applies to the construction of both Section 214 (a) (8) as to obsolescence of intangibles and Section 206 as to capital gain.

In case of doubt taxing statutes are to be construed most strongly against the Government and in favor of the citizen. *United States v. Wigglesworth,* 2 Story 368, 374; *United States v. Isham,* 17 Wall 496, 504; *Gould v. Gould,* 245 U. S. 151, 153; *United States v. Merriam,* 263 U. S. 179.

The rule applies as this is a deduction and not an exemption provision.

There seems to be a serious doubt as to the proper construction of Section 214 (a) (8) of the Revenue Act of 1918. The Commissioner of Internal Revenue, the Advisory Tax Board, the Rules and Regulations Section of the Bureau of Internal Revenue, and the Legal Department of the office of the Commissioner of Internal Revenue had no doubt whatsoever regarding the proper construction. Their construction uniformly was to the effect that the taxpayer was entitled to the deduction on account of obsolescence of intangibles, including good will. The United States District Court for Kentucky, if it had such doubt, resolved it in favor of the taxpayer in so far as intangibles, other than good will, was concerned. The conflicting opinions of the Circuit Courts of Appeals for the Second and Eighth Circuits certainly gave rise to a serious doubt as to the proper method of construction.

That doubt, we respectfully submit, if it exists in the minds of this Honorable Court, should be resolved in favor of the taxpayer.

CONCLUSION.

The petitioner had intangible assets consisting of good will, trade marks, trade brands, and trade names in both his distillery and wholesale liquor businesses which were worth $1,000,000.00 and $115,500.00, respectively, on March 1, 1913. On January 31, 1918, it was apparent that the value of the intangible assets would be destroyed or lost within a period of about four years. During such period the intangible assets were in the state of becoming obsolete—their value was being exhausted by lapse of time caused by prohibiting legislation. The said intangible assets were wholly destroyed by prohibition legislation. Petitioner should be allowed as a deduction from gross income a reasonable allowance for obsolescence, (the amount not being

disputed in the lower court) or in the alternative a deduction for the loss of the cost of such intangibles.

A similar deduction should be allowed petitioner for obsolescence of physical properties over the same period. The fact that medicinal whiskey was manufactured does not destroy the deduction. Obsolescence is not obsoleteness.

Petitioner owned the "Old Whiskey" personally. It was not part of his stock in trade. In any event he is entitled to the benefit of the capital gain provision because a business in forced liquidation under restrictions as to sale, with no means of replacement, has no stock in trade but only frozen capital assets.

The decision of the Circuit Court of Appeals herein should be reversed.

Respectfully submitted,

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APPENDIX.

Statutes.

Revenue Act of 1917, Act of October 3, 1917, ch. 63, Section 207 (a), 40 Stat. 300:

> Section 207. * * * "As used in this title 'invested capital' does not include stocks, bonds (other than obligations of the United States), or other assets, the income from which is not subject to the tax imposed by this title, nor money or other property borrowed, and means, subject to the above limitations: * * * Provided that * * * (b) *the good will, trade-marks, trade brands,* the franchise of a corporation or partnership, or other intangible property shall be included as invested capital * * *".

Revenue Act of 1918, Act of February 24, 1919, ch. 18, 40 Stat. 1057:

> Section 214: "(a) That in computing net income there shall be allowed as deductions (4) losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in a trade or business; * * *"
>
> * * * * * * *
>
> Section 214: "(a) That in computing net income there shall be allowed as deductions: (8) a reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence. In the case of such property acquired before March 1, 1913, this deduction shall be computed upon the basis of its fair market price or value as of March 1, 1913."

"Part V. Invested Capital. Section 325. (a) That as used in this title—

"The term 'intangible property" means patents, copyrights, secret processes and formulae, good will, trade-marks, trade brands, franchises, and other like property; * * *

"Section 326. (a) That as used in this title the term 'invested capital' for any year means (except as provided in subdivisions (b) and (c) of this section):

* * * * * * *

"(4) Intangible property bona fide paid in for stock or shares prior to March 3, 1917 * * *;

"(5) Intangible property bona fide paid in for stock or shares on or after March 3, 1917 * * *."

Revenue Act of 1921, Act of November 23, 1921, ch. 136, 42 Stat. 227:

Section 206: "(a) That for the purpose of this title: (6) The term 'capital assets' as used in this section means property acquired and held by the taxpayer for profit or investment for more than two years (whether or not connected with his trade or business), but does not include property held for personal use or consumption of the taxpayer or his family, or stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year."

Section 206: "(b) In the case of any taxpayer (other than a corporation) who for any taxable year derives a capital net gain, there shall (at the election of the taxpayer) be levied, collected and paid, in lieu of the taxes imposed by sections 210 and 211 of this title, a tax determined as fol-

lows: A partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner provided in sections 210 and 211, and the total tax shall be this amount plus 12½ per centum of the capital net gain: but if the taxpayer elects to be taxed under this section the total tax shall in no such case be less than 12½ per centum of the total net income. The total tax thus determined shall be computed, collected and paid in the same manner, at the same time and subject to the same provisions of the law, including penalties, as other taxes under this title."

* * * * * * *

Section 214: "(a) That in computing net income there shall be allowed as deductions: (8) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence. In the case of such property acquired before March 1, 1913, this deduction shall be computed upon the basis of its fair market price or value as of March 1, 1913."

Section 325 (a) and 326 (a) (4) (5) are the same as corresponding sections of the Revenue Act of 1918, supra.

with any provision of the National Prohibition Act or of this Act; but if any act is a violation of any of such laws and also of the National Prohibition Act or of this Act, a conviction for such act or offense under one shall be a bar to prosecution there for under the other. All taxes and tax penalties provided for in section 35 of Title II of the National Prohibition Act shall be assessed and collected in the same manner and by the same procedure as other taxes on the manufacture of or traffic in liquor.

If distilled spirits upon which the internal-revenue tax has not been paid are lost by theft, accidental fire, or other casualty while in possession of a common carrier subject to the Transportation Act of 1920 or the Merchant Marine Act, 1920, or if lost by theft from a distillery or other bonded warehouse, and it shall be made to appear to the commissioner that such losses did not occur as the result of negligence, connivance, collusion, or fraud on the part of the owner or person legally accountable for such distilled spirits, no tax shall be assessed or collected upon the distilled spirits so lost, nor shall any tax penalty be imposed or collected by reason of such loss, but the exemption from the tax and penalty shall only be allowed to the extent that the claimant is not indemnified against or recompensed for such loss. This provision shall apply to any claim for taxes or tax penalties that may have accrued since the passage of the National Prohibition Act or that may accrue hereafter. Nothing in this section shall be construed as in any manner limiting or restricting the provisions of Title III of the National Prohibition Act."

APPENDIX.

Willis Campbell Act of November 23, 1921, Chapter 134, Section 2, 42 Stat. 222.

"* * * No spirituous liquor shall be imported into the United States, nor shall any permit be granted authorizing the manufacture of any spirituous liquor, save alcohol, until the amount of such liquor now in distilleries or other bonded warehouses shall have been reduced to a quantity that in the opinion of the commissioner will, with liquor that may thereafter be manufactured and imported, be sufficient to supply the current need thereafter for all non-beverage uses: PROVIDED, That no vinous liquor shall be imported into the United States unless it is made to appear to the commissioner that vinous liquor for such non-beverage use produced in the United States is not sufficient to meet such non-beverage needs: PROVIDED FURTHER, That this provision against importation shall not apply to shipments en route to the United States at the time of the passage of this Act: And PROVIDED FURTHER, That the commissioner may authorize the return to the United States under such regulations and conditions as he may prescribe any distilled spirits of American production exported free of tax and reimported in original packages in which exported and consigned for redeposit in the distillery bonded warehouse from which originally removed."

Treasury Department Rulings.

Treasury Department Bureau of Internal Revenue

BULLETIN "F"
INCOME TAX.

DEPRECIATION AND OBSOLESCENCE.

REVENUE ACT OF 1918.

This bulletin contains information from which taxpayers and their counsel may obtain the best available indication of the trend and tendency of official opinion in the administration of the income and profits tax provisions of the Revenue Act of 1918, with respect to depreciation and obsolescence. It does not have the force or effect of a Treasury Decision and does not commit the Department to any interpretation of law which has not been formally approved and promulgated by the Secretary of the Treasury.

Taxpayers and officers of the Bureau of Internal Revenue are cautioned against reaching a conclusion in any case merely on the basis of similarity to conditions stated herein and should base their judgment on the application of all pertinent provisions of the law, regulations, and other Treasury Decisions to all of the facts in each case.

[Seal—Office of
Commissioner of
Internal Revenue]

WASHINGTON
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1920

INTRODUCTION.

The contents of this bulletin indicate the trend and tendency of official opinion in the Bureau of Internal Revenue in administering the portions of the Revenue Act of 1918 which provide for the deduction from gross income of reasonable allowances for exhaustion, wear and tear, and obsolescence of property used in trade or business. The subject matter includes Treasury Decisions, Opinions of the Solicitor of Internal Revenue, the Advisory Tax Board and the Committee on Appeals and Review, portions of Regulations 45 and other information of a general nature.

Since obsolescence was not recognized for income-tax purposes prior to the passage of the Revenue Act of 1918, comparatively few rulings have been made on that subject. This bulletin, however, contains several opinions rendered by the Advisory Tax Board relating to intangible assets and other property rendered obsolete by prohibition legislation.

The Bureau does not prescribe rates to be used in computing depreciation and obsolescence, as it would be impracticable to determine rates which would be equally applicable to all property of a general class or character. For this reason no table of rates is published. The rate applicable and the adjustment of any case must depend upon the actual conditions existing in that particular case.

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DEPRECIATION OF INTANGIBLE PROPERTY. — Intangibles, the use of which in the trade or business is definitely limited in duration, may be the subject of a depreciation allowance. Examples are patents and copyrights, licenses and franchises. Intangibles, the use of

which in the business or trade is not so limited, will not usually be a proper subject of such an allowance. If, however, an intangible asset acquired through capital outlay is known from experience to be of value in the business for only a limited period, the length of which can be estimated from experience with reasonable certainty, such intangible asset may be the subject of a depreciation allowance, provided the facts are fully shown in the return or prior thereto to the satisfaction of the Commissioner. The words "capital outlay" used in this paragraph mean cash, other property, or corporate stock given in exchange for the intangibles.

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OBSOLESCENCE OF INTANGIBLES. — Obsolescence is not ordinarily applicable in the case of intangibles but will be allowed in exceptional cases, as in the case of the discontinuance of a going business because of the exhaustion of its source of supply, where the cost of the good will, or its value as of March 1, 1913, if acquired prior to that date, can be definitely shown and the period of its obsolescence determined with reasonable accuracy.

To sustain a claim for deduction for obsolescence of good will, it must be shown that the good will will be of no value at the close of an approximately definite period, and that the taxpayer will be forced to discontinue the business and be unable to continue in another similar business.

An allowance for obsolescence of good will will be made only in connection with such good will as is assignable, as distinguished from good will attaching to individuals owning or conducting a business or to the premises at which it is or was conducted; and no allowance for obsolescence will be granted in any case where, in connection with the operation of the business, the

good will will be valuable in another business after the termination of the business in which the taxpayer is engaged.

* * * * * * * *

BOTTLE MANUFACTURING PLANTS. — Property consisting of a plant, including equipment, for the manufacture of beer bottles, which because of prohibition legislation has lost its usefulness and can not be sold has, to the extent the property or plant was constructed for the manufacture of beer bottles and is not suited or adapted for any other [p. 15] purposes without reconstruction, become obsolete, and the taxpayer to that extent is entitled to a deduction for obsolescence. That part of the shrinkage in value of the plant, if any, which is not thus due to obsolescence may not be claimed as a deduction for loss until the property is sold or becomes worthless and the loss is definitely ascertained.

PROPERTY OF BREWERS AND DISTILLERS.—The same principle stated in the case of bottle manufacturing plants is applicable in the case of other property or equipment of distillers, brewers, and liquor dealers which has been impaired in value through prohibition legislation. The loss in value may be established by evidence other than the actual sale of the obsolete property.

INTANGIBLE ASSETS OF BREWERS, DISTILLERS, AND DEALERS IN LIQUOR.—In Advisory Tax Board Memorandum 44 (Cumulative Bulletin, December, 1919, p. 133) it was held that distillers and dealers in liquor are entitled to make a deduction (based upon actual cost or fair market value as at March 1, 1913) from gross income, on account of depreciation or obsolescence of their intangibles, such as good will, trademarks, trade brands, etc., such deduction being limited to assignable assets, the value of which has been destroyed by prohibition legislation, and that in arriving at the taxable

income for the first taxable year ending on or after January 31, 1918, the obsolescence fully accrued on that date is to be allowed as a deduction in computing the income subject to taxation under the Revenue Act of 1918, plus a further deduction of such proportion of the remaining value of the intangible assets as the interval between January 31, 1918, and the end of the taxable year bears to the total interval between January 31, 1918, and January 16, 1920 (unless at an earlier date the taxpayer discontinues his business in which case such earlier date shall mark the close of the period), and that for any taxable year following the taxable year just referred to a deduction in respect of the value of such intangible assets on January 31, 1918, based upon a ratable distribution, will be permissible. This paragraph applies also to brewers.

23-19-545.
T. D. 2929.

Section 214 (a) 8, Article 163: Depreciation of intangible property.

MODIFICATION OF ARTICLE 163, REGULATIONS NO. 45—DEPRECIATION OF INTANGIBLE PROPERTY.

Article 163. Regulations 45, is modified to read as follows by eliminating therefrom the last sentence reading, "There can be no such allowance in respect of good will, trade names, trade-marks, trade brands, secret formulae, or processes":

Art. 163. *Depreciation of intangible property.*—Intangibles, the use of which in the trade or business is definitely limited in duration, may be the subject of a depreciation allowance. Examples are patents and copyrights, licenses and franchises. Intangibles, the use of which in the business or trade is not so limited,

will not usually be a proper subject of such allowance. If, however, an intangible asset acquired through capital outlay is known from experience to be of value in the business for only a limited period, the length of which can be estimated from experience with reasonable certainty, such intangible asset may be the subject of a depreciation allowance, provided the facts are fully shown in the return or prior thereto to the satisfaction of the commissioner.

15-19-445.
T. B. R. 44.

Section 214 (a) 8, Article 163: Depreciation of intangible property.

Obsolescence upon intangible assets such as good will, trade-marks, or trade brands may be deducted, within certain definite limitations in computing taxable net income.

In an office letter to A, it is held that distillers and dealers in liquors are entitled in computing taxable net income to deduct a reasonable allowance for obsolescence of good will, trade-marks, or trade brands, the value of which has been impaired or destroyed by prohibition legislation, such deduction to be computed upon the basis of a period beginning on November 21, 1918, the date upon which the Agricultural appropriation act providing for war-time prohibition was enacted, and July 1, 1919, the date upon which war-time prohibition was to become effective. It was further held (a) that to sustain a claim for a deduction for obsolescence in respect of good will, trade-marks, or trade brands, the taxpayer must show that the value of the property in question has been destroyed or will be destroyed by prohibition legislation, and that the taxpayer is not continuing in any similar trade or busi-

ness; (b) that an allowance will be made only in respect of such assets as are assignable as distinguished from those attaching to individuals owning or conducting the business, or to the premises at which it is being or has been conducted; and (c) that no allowance for obsolescence will be made in any case where in connection with the operation of his previous business, the taxpayer has developed a good will, trademark, or trade brand that will be valuable in continuing a lawful business after prohibition becomes effective.

A has appealed to the Commissioner claiming that the above decision errs in limiting the period over which the obsolescence may be spread from November 21, 1918, to June 30, 1919. He takes the position "That the depletion by obsolescence is the result of the Federal prohibition process, which has been in the course of development * * *;" that although "The trade made substantial apparent profits in 1918" this resulted merely from the liquidating of inventories, and "trade was garnering apparent profits which in reality were only the salvaging of capital * * *;" and urges that if a fixed obsolescence period is to be stated, "The Department conclude that December 18, 1917, the date of the action of the House of Representatives which constituted the final submission of national prohibition to the States, be taken as the point of commencement of the obsolescence."

The question raised, therefore, is whether the period during which the obsolescence may be spread should be limited to that beginning on November 21, 1918, or should be taken as from December 18, 1917, the date upon which Congress submitted the prohibition amendment to the States.

Before considering this question directly, it seems desirable to examine the grounds upon which obsoles-

cence of intangibles, such as good will, trade-marks, trade brands, etc., may be allowed. In the accounting required for tax purposes intangibles, such as good will, trade-marks, and the like are distinguished from tangible property in that in the ordinary case a taxpayer is not required or permitted to make current deductions for depreciation, including in this term ordinary obsolescence. This distinction rests upon the ground that in the ordinary case depreciation of intangibles is too indefinite and uncertain to be reduced to terms of money. In specific instances, however, intangibles may be brought within the rule applicable to tangible property, but only by the force of unusual and controlling circumstances. Article 163 of Regulations 45, for instance, states that "Intangibles, the use of which in the trade or business is definitely limited in duration, may be the subject of a depreciation allowance." It is true that this same article states that no such allowance may be made in the case of intangibles of the class now under consideration, and while in general this negative decision is sound, the controlling rule is the one quoted above, and when an item of intangible property falls within that rule it must be dealt with accordingly. The major rule laid down in article 163 is a reasonable extension of the provision of article 143 covering loss of useful value. This article provides "When through some change in business conditions the usefulness in the business of some or all of the capital assets is suddenly terminated, so that the taxpayer discontinues the business or discards such assets permanently from use in the business, he may claim as a loss for the year in which he takes such action the difference between the cost or the fair market value as of March 1, 1913, of any asset so discarded (less any depreciation allowance) and its salvage value remaining * * *."

The question next arises whether an intangible acquired at a date when its useful life is indefinite may become the subject of a depreciation allowance at some subsequent date at which time the duration of its useful life becomes definitely known. If so, the loss which might be claimed at the end of the life may be spread over the term of the remaining useful life. To hold that no such spread is allowed it is necessary to construe the first sentence of article 163 as meaning that only those intangibles the useful life of which is known at the time of acquisition to be definitely limited in duration may be the subject of depreciation allowance. This seems to be a strained construction, and in the light of article 143 is unnecessarily harsh. The reasonable conclusion seems to be, therefore, that when it is demonstrated that the useful life of an intangible is definitely limited, such intangible then becomes a proper subject of depreciation allowance.

Applying these considerations to the intangibles belonging to distillers and dealers in liquors it is found that such intangibles are subject to depreciation (or obsolescence) during the period in which it is known that their useful life is definitely limited in duration. The determination of this period is, however, by no means easy. Looking backward it can now be seen that prohibition has during recent years had a rapid growth in this country, particularly in the South and in the West. Before the constitutional amendment was adopted some 33 States had prohibition legislation and local option was similarly effective in substantial parts of many of the other States. As early as March, 1913, the Webb-Kenyon Act gave strong indication of a growing sentiment, and this sentiment has since been registered in many other political and judicial expressions.

However clear the general implication of these

facts may have been, nothing throughout this course of events was sufficiently explicit and final to fix a period at the end of which the property now under consideration would become valueless. Among these indefinite or incomplete events the submission by Congress of the eighteenth amendment on December 18, 1917, stands out as the most far-reaching and important in the entire chain. The fact that this legislation was adopted in both Houses of Congress by large majorities gave at least some indication of the probable reception of the proposed amendment by the States, and it may, therefore, be granted that at the date of submission there was substantial reason to believe that the amendment would be adopted by the States.

There was, however, no certainty upon this point, and the leaders on both sides of the controversy showed plainly by their actions at the time that neither believed that the issue was settled. Were it not for the facts surrounding the submission of the constitutional amendment, a satisfactory date would be fixed by the adoption of the war-time prohibition act on November 21, 1918. Standing alone this date could be accepted as marking the beginning of the period during which the trade-marks, trade brands, and good will of distillers and dealers in liquors would be completely exhausted. The prohibition amendment, while not finally adopted until after the enactment of war-time prohibition had, however, made such progress that before that date its adoption became a foregone conclusion. The attitude of many States was known, and the formal act of ratification merely awaited the assembling of the legislatures. The trend of sentiment was early shown by the action of several States upon which the distillers and dealers in liquors were counting for success, and which were classed as doubtful by the prohibition forces. Thus in January, 1918, Massachusetts, Mary-

land, and Kentucky, the first two of which were considered very doubtful by the prohibitionists, voted in favor of the prohibition amendment by a decisive vote. Louisiana, another doubtful State, deadlocked in January upon the amendment, and later in the year ratified. It seems certain that an unprejudiced observer would, in view of the history of the movement and the decisive action taken by these doubtful States in January, have concluded that prohibition was a certain event, which, under the terms of the amendment, would become effective within a year from its final adoption. The conclusion is, therefore, reached that it is reasonable to allow distillers and dealers in liquors to make a deduction in computing net income under the provisions of the Revenue Act of 1918, for any taxable year ending on or after January 31, 1918, and that the end of the period be fixed at the date upon which a taxpayer engaged as distiller or dealer in liquors discontinues such business, such date being in no case later than January 16, 1920, the date upon which prohibition by constitutional amendment becomes effective.

A further question remains for consideration. Upon what basis should the deduction for obsolescence be apportioned between the taxable years ending after January 31, 1918? The statute, sections 214 (a) (8) and 234 (a) (7), provides for a "reasonable" allowance. This places upon the department the burden of laying down rules and regulations defining, so far as may be done, what is "reasonable." In the great majority of cases depreciation is fairly measured by the effluxion of time. This is the ordinary rule, a departure from which should be allowed only when the deduction provided thereunder does not meet the statutory requirement of reasonableness. The use in the statute of the word "reasonable" clearly implied that no rigid rule applicable to all cases can be laid down.

Observation of individual cases amply proves that this is true, and therefore when the ordinary rule does not produce a reasonable result, the statute requires that another and a reasonable method be adopted in a particular case or class of cases. The situation presented by the distillers and dealers in liquors is highly exceptional. The total amount in respect of which they are entitled to claim a deduction is the cost of their good will, trade-marks, trade brands, or the value thereof, on March 1, 1913, if acquired prior thereto, excluding, of course any intangibles acquired since that date, the expenditures for which were deductible in computing income for tax purposes. But as already indicated, the legislative situation had by January 31, 1918, reached a decisive point which completed the first stage in the obsolescence of these assets. On that date a computable part thereof had become obsolete. The value of such assets rests upon the probable future income that will accrue to the owner thereof. Estimates of the probable amount of this income may vary, but there is no other known method by which the value can be computed. In view of the status of prohibition legislation on January 31, 1918, it is certain that upon that date the value of the good will, trade-marks, trade brands, etc., of distillers and dealers in liquors was reduced to the then present value of the income to be derived therefrom between that date and approximately January, 1920. Whatever this value might be in a given case, it would be different from, and probably much less than, the value on March 1, 1913. Had prohibition been immediately effective, instead of becoming operative at a future date, these taxpayers would have been entitled to deduct from gross income of any taxable period ending on or after January 31, 1918, the entire amount of such intangibles.

Depreciation of intangibles now in question when

computed upon the basis of the time rule does not meet the requirements of the statute, and therefore another rule must be found. For some purposes apportionment based upon the relative profits of two or more taxable periods provides a proper method, but this rule is obviously inapplicable to the cases now under consideration. The rule of apportionment which most closely approximates the actual facts, and is therefore the most reasonable, is that under which the value of the intangibles on January 31, 1918, is spread on the time basis between that date and the date upon which prohibition became effective and the balance of the allowable deduction (measured by the difference between the value on January 31, 1918, and March 1, 1913), taken in accordance with the provisions of section 205 of the act and articles 1621-1625 of Regulations 45 against the first taxable year ending on or after January 31, 1918.

It is, therefore, the opinion of the Advisory Tax Board (1) that distillers and dealers in liquors are entitled to make a deduction (based upon actual cost or fair market value as at March 1, 1913) from gross income, on account of depreciation or obsolescence of their intangibles, such as good will, trade-marks, trade brands, etc., such deduction being limited to assignable assets, the value of which has been destroyed by prohibition legislation, and (2) that in arriving at the taxable income for the first taxable year ending on or after January 31, 1918, the obsolescence fully accrued on that date is to be allowed as a deduction in computing the income subject to taxation under the revenue act of 1918, plus a further deduction of such proportion of the remaining value of the intangible assets as the interval between January 31, 1918, and the end of the taxable year bears to the total interval between January 31, 1918, and January 16, 1920 (unless at an earlier date the taxpayer discontinues his business, in

which case such earlier date shall mark the close of the period), and (3) that for any taxable year following the taxable year just referred to a deduction in respect of the value of such intangible assets on January 31, 1918, based upon a ratable distribution, will be permissible.

24-19-565.
O. D. 298.

Section 214 (a) 8, Article 163: Depreciation of intangible property.

Deductions from gross income on account of depreciation or obsolescence of intangibles, such as good will, trade-marks, and trade brands, allowed distillers and dealers in liquors, are also applicable to brewers.

30-19-640.
O. D. 344.

Section 214 (a) 8, Article 163: Depreciation of intangible property.

Depreciation of intangible property as explained in article 163 of Regulations 45 applies to all intangible property including patents and copyrights, whether acquired for cash, other property, or corporate stock. The term "capital outlay" includes corporate stock.

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No. 114

In the Supreme Court of the United States

OCTOBER TERM, 1929

FREDERICK C. RENZIEHAUSEN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

MEMORANDUM FOR THE COMMISSIONER OF INTERNAL REVENUE

U. S. GOVERNMENT PRINTING OFFICE: 1929

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PREVIOUS OPINIONS

The opinion of the United States Board of Tax Appeals is reported in 8 B. T. A. 87. (R. 31.) The opinion of the United States Circuit Court of Appeals for the Third Circuit is reported in 31 F. (2d) 675. (R. 137.)

JURISDICTION

The judgment of the United States Circuit Court of Appeals sought to be reviewed was entered on March 7, 1929 (R. 142–143), and petition for writ of certiorari was filed in this Court on May 27,

1929. Jurisdiction to issue a writ is found in Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

STATEMENT

The petitioner was engaged, under the trade name of Large Distilling Company, in the business of distilling rye whiskey, and was also a partner in the firm of Schuetz, Renziehausen & Company (R. 34), which was engaged in the wholesale liquor business. Both businesses owned considerable property, real and personal. (R. 40, 42–43.) They also owned certain trade-marks, trade brands, trade-names, and good-will, having a monetary value. (R. 36–38.) Because of the war-time prohibition legislation, the National Prohibition Amendment and laws enacted in pursuance thereof, they were forced to curtail or suspend their activities as distillers of intoxicating liquors. (R. 39, 43.) Petitioner claimed deductions from gross income for income-tax purposes in the years 1918, 1919, 1920, and 1921 because of obsolescence of both tangible and intangible property alleged to have been caused thereby. (R. 5–18.) He also claimed that Section 206 of the Revenue Act of 1921 (R. 5–18), providing for the computation of capital gain, was applicable to the disposal of their stocks of liquor. This contention is based on the theory that they could no longer regularly engage in the liquor business and consequently that the sale of such liquor as they had was an isolated rather than

a recurring transaction. Petitioner also claimed, as an alternative to the claim for obsolescence of intangibles, that he was entitled to deduct the loss, under Section 214 (a) (4) of the Revenue Act of 1918, of value of the trade-marks, trade brands, trade names, and good will.

The Commissioner of Internal Revenue disallowed all of these claims. (R. 22–24.) The Board of Tax Appeals allowed certain deductions for obsoleteness of certain of the tangible properties which it found occurred in the year 1921, but decided in favor of the Commissioner as to the other questions involved. (R. 44–56.) Upon appeal to the Circuit Court of Appeals the decision of the Board of Tax Appeals was affirmed, and from that decision the petitioner has applied for a writ of certiorari from this Court to the Circuit Court of Appeals for the Third Circuit.

CONCLUSION

The most important of the questions urged by the taxpayer is with respect to his right to take a deduction for the obsolescence of intangible personal property. The Circuit Court of Appeals decided this question in accordance with the decisions of the Circuit Courts of Appeals for the Eighth Circuit in *Red Wing Malting Co.* v. *Willcuts, Collector,* 15 F. (2d) 626; certiorari denied, 273 U. S. 763, and for the Ninth Circuit in *Landsberger* v. *McLaughlin, Collector,* 26 F. (2d) 77. The decision is contrary to that of the Circuit Court of Appeals for

the Second Circuit in *Haberle Crystal Springs Brewing Co.* v. *Clarke, Collector,* 30 F. (2d) 219, in which this Court has granted a writ of certiorari, the case now being No. 68 of the October Term, 1929. The opinion of the Circuit Court of Appeals for the Third Circuit in the instant case was quoted in full as an appendix to the brief in support of the petition of the Collector for writ of certiorari in the *Haberle Crystal Springs Brewing Company Case.*

We believe the decision of the Circuit Court of Appeals in the instant case to be correct on all of the questions involved. Since, however, the question of the allowability of a deduction for obsolescence of intangible personal property is now before this Court in the *Haberle Crystal Springs Brewing Company Case,* though on somewhat different findings of fact, the issuance of a writ of certiorari herein would save the petitioner's rights pending its decision, and we see no reason to oppose it.

Respectfully submitted.

CHARLES E. HUGHES, Jr.,
Solicitor General.
J. LOUIS MONARCH,
JOHN VAUGHAN GRONER,
Special Assistants to the Attorney General.

JULY, 1929.

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No. 114

In the Supreme Court of the United States

OCTOBER TERM, 1929

FREDERICK C. RENZIEHAUSEN, PETITIONER

v.

ROBERT H. LUCAS, AS COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR RESPONDENT

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In the Supreme Court of the United States

OCTOBER TERM, 1929

No. 114

FREDERICK C. RENZIEHAUSEN, PETITIONER

v.

ROBERT H. LUCAS, AS COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR RESPONDENT

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 39) is reported in 8 B. T. A. 87. The opinion of the United States Circuit Court of Appeals for the Third Circuit (R. 113) is reported in 31 F. (2d) 675.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on March 7, 1929. (R. 118–119.) Petition for certiorari was filed May 27, 1929. (R. 121.) Certiorari was granted October 14,

1929. (R. 120.) Jurisdiction is conferred upon this Court by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

Petitioner was engaged in the business of distilling and selling whiskey, and also in the wholesale liquor business. The Eighteenth Amendment was ratified by the requisite number of States January 16, 1919, and became effective January 16, 1920. The National Prohibition Act became effective January 16, 1920, and the Willis-Campbell Act November 23, 1921. The distillery ceased operations upon the passage of the Willis-Campbell Act. The questions are:

(1) Whether any portion of the March 1, 1913, value of petitioner's good will, trade marks, trade brands, or trade names is deductible for the years 1918 to 1921, inclusive (as respects the wholesale liquor business the period is 1918 to 1920), under the statutory allowance for "exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence."

(2) An alternative question is whether petitioner suffered a loss in the year 1919 of the good will, trade marks, trade brands, or trade names of the distillery business, which may be deductible under Section 214 (a) (4) of the Revenue Act of 1918. If so, the further question arises whether petitioner has shown the cost of such assets.

(3) Whether the taxpayer under the facts is entitled to deductions for obsolescence of plant and equipment of his distilling business for the years 1918 to 1921, inclusive, under Section 214 (a) (8) of the Revenue Acts of 1918 and 1921.

(4) Whether the taxpayer is entitled to have taxed as a capital gain under Section 206 of the Revenue Act of 1921 the profits realized on the sale in 1922 of certain old whiskey which he had held since its manufacture in his business more than two years prior to 1922.

STATUTES INVOLVED

Revenue Act of 1918, 40 Stat. 1057, 1066, 1067:

> SEC. 214. (a) That in computing net income there shall be allowed as deductions:
>
> * * * * *
>
> (4) Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in trade or business;
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> * * * * *
>
> (8) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence;
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> * * * * *

Revenue Act of 1921, c. 136, 42 Stat. 227, 232, 233, 239, 240:

> SEC. 214. (a) That in computing net income there shall be allowed as deductions:
>
> * * * * *
>
> (8) A reasonable allowance for the exhaustion, wear and tear of property used in

the trade or business, including a reasonable allowance for obsolescence. In the case of such property acquired before March 1, 1913, this deduction shall be computed upon the basis of its fair market price or value as of March 1, 1913;

* * * * *

SEC. 206. (a) That for the purpose of this title:

(1) The term " capital gain " means taxable gain from the sale or exchange of capital assets consummated after December 31, 1921;

(2) The term "capital loss" means deductible loss resulting from the sale or exchange of capital assets consummated after December 31, 1921;

(3) The term "capital deductions" means such deductions as are allowed under this title for the purpose of computing net income and are properly allocable to or chargeable against items of capital gain as defined in this section;

(4) The term "capital net gain" means the excess of the total amount of capital gain over the sum of the capital deductions and capital losses;

(5) The term "ordinary net income" means the net income, computed in accordance with the provisions of this title, after excluding all items of capital gain, capital loss, and capital deductions; and

(6) The term "capital assets" as used in this section means property acquired and held by the taxpayer for profit or investment

for more than two years (whether or not connected with his trade or business), but does not include property held for the personal use or consumption of the taxpayer or his family, or stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year.

(b) In the case of any taxpayer (other than a corporation) who for any taxable year derives a capital net gain, there shall (at the election of the taxpayer) be levied, collected and paid, in lieu of the taxes imposed by sections 210 and 211 of this title, a tax determined as follows:

A partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner provided in sections 210 and 211, and the total tax shall be this amount plus 12½ per centum of the capital net gain; but if the taxpayer elects to be taxed under this section the total tax shall in no such case be less than 12½ per centum of the total net income. The total tax thus determined shall be computed, collected and paid in the same manner, at the same time and subject to the same provisions of law, including penalties, as other taxes under this title.

* * * * *

STATEMENT

The taxpayer, Frederick C. Renziehausen, is a resident of Pittsburgh, Pennsylvania, and during the taxable years and prior thereto was the sole

owner of the whiskey distilling business conducted under the trade name of the Large Distilling Company. He also owned a one-half interest in the partnership of Schuetz, Renziehausen & Company, wholesale liquor dealers, Pittsburgh. (R. 31.)

In 1796 a whiskey-distilling business was founded by Jonathan Large under the trade name of the Large Distilling Company. From 1884 to 1897 this business was conducted as a partnership, composed of Henry Large, his wife, and the taxpayer. In 1897 the taxpayer became the sole owner of the business and thereafter conducted it as a sole proprietorship. (R. 31.)

The business of the Large Distilling Company was principally that of distilling whiskey, which it sold to wholesale liquor dealers under uniform contracts. It also carried on a warehousing business, storing the whiskey which it distilled in its bonded warehouses until matured and withdrawn by the owners, for which the latter paid certain monthly storage charges. It also bottled and cased the matured whiskey in bond, for which it received compensation from the owners thereof. At various times it purchased warehouse receipts for whiskey in its own bonded warehouses and resold the same at a profit. It carried the whiskey left over from each distilling season to various stages of maturity, and as opportunities were afforded disposed of it to the trade. (R. 31.)

The whiskey was sold under contract prior to the time it was distilled. The whiskey was distilled in the fall and spring after the contracts were

made and was placed in Government bonded warehouses and the warehouse certificates turned over to the owners of the whiskey according to the quantities purchased. After the whiskey had remained in the warehouses for the time required by the Government regulations, usually four years, it was bottled in bond under Government supervision by the Large Distilling Company for the owners. (R. 32–33.)

"Large" whiskey, by which name the product of the Large Distilling Company was generally known, was distributed by wholesale and retail liquor dealers throughout the United States. It was generally regarded by the wholesale trade as one of the leading rye whiskeys of the country. Until the Large Distilling Company ceased distilling for beverage purposes in 1917, there had been a steady growth in the demand for its product. The company seldom operated its distillery to its full capacity. The practice was to determine upon the quantity of whiskey to be distilled in the following season before soliciting contracts. The quantity specified in the contract of a particular wholesale dealer was usually based upon the quantity upon which that dealer was making tax payments. The purpose of this method was to prevent as far as practicable speculation in warehouse receipts for "Large" whiskey. Because of these practices, the demand for the product generally exceeded the supply. (R. 33.)

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Between 1899 and 1913, the Large Distilling Company expended for advertising the sum of $82,500.02, and between 1914 and 1921, inclusive, it expended for the same purpose the sum of $86,155.61. (R. 33.)

In addition to the amounts expended for advertising, the Large Distilling Company, between 1899 and 1913, inclusive, paid its customers the total sum of $55,781.10 for leakage, and between 1914 and 1921, inclusive, it expended for that purpose the total sum of $13,300.14. Leakage refers to the evaporation while the whiskey is stored in the Government bonded warehouses in excess of the Government allowance and upon which the owners of the whiskey were required to pay the tax. The tax on excess evaporation was paid by the owners, and they were reimbursed by the Large Distilling Company, although there was no specific provision in the contracts under which the company could be held liable. (R. 33–34.)

On July 19, 1897, the Large Distilling Company purchased a trade-mark for $5,000 cash. On March 1, 1913, the Large Distilling Company owned five trade-marks or trade names. (R. 34.) The petitioner was not paid any salary for his personal services from the time he became a partner in the Large Distilling Company in 1884 to and including the year 1912. The Board found that a reasonable compensation for the period between 1908 and 1912, inclusive, for the services he rendered would have been $15,000 per annum. (R. 35.)

The last whiskey produced by the Large Distilling Company for beverage purposes was distilled in May, 1917. Distilling ceased then because of war-time prohibition. The taxpayer believed in 1918 that because of war-time prohibition and the progress which had been made towards the adoption of the Eighteenth Amendment the distilling part of the business of the Large Distilling Company was ended and the business would be wound up and liquidated within four years. In 1919 the petitioner became aware that he could manufacture whiskey for medicinal purposes and in the fall of that year the Large Distilling Company resumed distilling operations for the production of whiskey for medicinal purposes and continued such operations until about November 23, 1921. On November 23, 1921, Congress enacted the so-called Willis-Campbell Act, c. 134, 42 Stat. 222, which provided in effect that whiskey could be manufactured for medicinal purposes only under permits issued by the Commissioner of Internal Revenue. No permit was obtained by the taxpayer for distilling thereafter and at the time of the hearing of this case before the Board no permits had been issued under the Willis-Campbell Act. (R. 35–36.)

The Large Distilling Company manufactured whiskey for medicinal purposes in 1919 in the amount of 396 barrels, in 1920 in the amount of 5,858 barrels, and in 1921 in the amount of 10,400 barrels. (R. 36.)

Of the physical properties of the Large Distilling Company none, except the bonded warehouses, have been put to any use since about November 23, 1921. The Board found that the salvage value of the physical properties, not including the bonded warehouses, was $19,375. The four bonded warehouses owned by the Large Distilling Company were of the rack type of construction for the storage of whiskey in barrels and were not adaptable to any other purpose. Their total capacity was 55,000 barrels. All four of the warehouses were being used for the storage of whiskey as late as 1923 and at all times during the taxable years. (R. 37.)

Prior to January 1, 1918, the Large Distilling Company disposed of the whiskey it manufactured in bulk to the wholesale liquor trade. The sales made after that date have been made to persons holding Government permits to purchase whiskey for medicinal purposes and have consisted entirely of bottled-in-bond whiskey. (R. 37.)

The firm of Schuetz, Renziehausen & Company was founded in 1879, and after 1892 until it was liquidated in 1925 the business was carried on by Schuetz and the petitioner. The business of the partnership was that of wholesale liquor dealers, selling brandies, cordials, fine liquors, and wines. At March 1, 1913, and thereafter until the adoption of the Eighteenth Amendment, the firm enjoyed the patronage of the most substantial retailers in the territories in which it did business.

On March 1, 1913, the firm owned registered trademarks for "Fort Pitt Whiskey," "Diamond Monogram Whiskey," and "Crusader Dry Gin." (R. 37–38.)

In 1908 there was opened on the books of the Large Distilling Company an account designated "old whiskey." At the close of each distilling season the whiskey manufactured and not sold was charged to this account and carried to maturity when it was sold to the trade through the organization of the Large Distilling Company. In 1922 all of the whiskey then carried in this account was sold. It had all been held for profit for more than two years prior thereto. The Commissioner refused to tax the profit from the sale of this whiskey as a capital gain at the rate of 12½% under the provisions of Section 206 of the Revenue Act of 1921. (R. 39.)

The Commissioner further disallowed deductions claimed for obsolescence of the tangible and intangible property of the distilling business for the years 1918 to 1921, inclusive, deductions claimed for loss of such intangibles for the year 1919, and those claimed for obsolescence of the intangible properties of the wholesale liquor business for the years 1918 to 1920, inclusive. (R. 30.) The Board of Tax Appeals held that the tangible property of the distilling business, except the warehouses, became obsolete in 1921 and that the petitioner was entitled to deduct from income for that year as a loss the

depreciated cost of such property less the salvage value. The Board also allowed deductions for obsolescence of the warehouses in 1921 and 1922 measured by the decrease in useful value thereof in those years. All other deductions disallowed by the Commissioner were sustained by the Board. Upon review taken by both the petitioner and the respondent the Circuit Court of Appeals for the Third Circuit affirmed the decision of the Board.

SUMMARY OF ARGUMENT

The respondent contends that the Board of Tax Appeals and the appellate court below correctly held that no deduction for obsolescence of the good will, trade-marks, trade brands and trade names of the distilling business or the wholesale liquor business was allowable inasmuch as the obsolescence deduction provided by Section 214 (a) (8) of the Revenue Acts of 1918 and 1921 was not intended to apply to intangibles such as good will. The argument in support of this view is identical with that presented in the brief for the collector in the case of *Clarke, Collector* v. *The Haberle Crystal Springs Brewing Company,* No. 68, October Term, 1929. It was therein contended that in enacting the various Excise or Revenue Acts from 1909 until the Revenue Act of 1918, Congress provided for deduction from income for depreciation only on account of those assets which were consumed or used up in the taxpayer's trade or business and that in enacting the Revenue Act of 1918, Congress did not intend to

extend the scope of the depreciation deduction but meant to confine it to wasting assets; that by including an allowance for obsolescence in the depreciation deduction under the Revenue Act of 1918 it was not the legislative intent to add any new species of property to that previously subject to the depreciation allowance and that the obsolescence deduction there provided for wasting assets does not apply to such an intangible property as good will.

Even if an obsolescence deduction were allowable in respect of good will and the kindred intangibles, such deduction can not properly be allowed in this case with respect to the intangibles of the distilling business, since during the years for which the deduction was claimed there was no obsolescence in fact.

The petitioner is not entitled to a deduction in the year 1919 under Section 214 (a) (4) of the Revenue Act of 1918 for loss based on the cost of the intangibles of the distilling business. During 1919 and 1920 and until late in 1921, the petitioner continued to manufacture whiskey and to sell his product to those permitted to buy for medicinal purposes. The business was not abandoned during the year 1919, and the good will was not discarded or destroyed. No loss was sustained during the year within the meaning of Section 214 (a) (4). Even if a loss deduction were allowable in the year 1919, the petitioner has not proved the cost of the intangible assets as the basis for the amount to be allowed.

Deductions claimed for obsolescence of the tangible properties of the distilling business for the years 1918, 1919, and 1920 were properly disallowed. The Board permitted a deduction for the year 1921 of the depreciated cost of the plant and its equipment less the salvage value as a loss sustained by abandonment due to obsoleteness and also allowed a deduction for obsolescence of warehouses in 1921 and 1922. The evidence supports the view of the Board and the Circuit Court of Appeals that obsoleteness of the tangible property was not foreseen in 1918, 1919, or 1920. As the petitioner bore the burden of proof it was incumbent upon him to show that obsoleteness could have been foreseen in these years. *United States* v. *Rindskopf,* 105 U. S. 418; *Wickwire* v. *Reinecke,* 275 U. S. 101. In the absence of proof of this material fact the disallowance of the deduction should be sustained. *Botany Mills* v. *United States,* 278 U. S. 282.

The "old whiskey" sold by the petitioner in 1922 was not a capital asset; it represented a product of his capital and labor, manufactured for sale and not acquired for profit or investment, and was stock in trade which would properly be included in his inventory. Therefore, the profits realized on the sale of a portion thereof in 1922 were not to be taxed under the capital gain provisions of Section 206 of the Revenue Act of 1921.

ARGUMENT

I

THE PETITIONER IS NOT ENTITLED TO ANY DEDUCTION FOR THE YEARS 1918, 1919, 1920, AND 1921 FOR OBSOLESCENCE OF TRADE-MARKS, TRADE BRANDS, TRADE NAMES, OR GOOD WILL OF THE LARGE DISTILLING COMPANY OR OF THE FIRM OF SCHUETZ, RENZIEHAUSEN & COMPANY

The petitioner contends that as the owner of the entire business of the Large Distilling Company he is entitled, under Section 214 (a) (8) of the Revenue Acts of 1918 and 1921, to a deduction from income for the years 1918, 1919, 1920, and 1921, for obsolescence of the good will, trade-marks, trade brands, and trade names of the business resulting from Federal prohibition legislation, such deduction to be based upon a March 1, 1913, value of those intangibles in the amount of $1,000,000. He also claims the right to an obsolescence deduction in the years 1918, 1919, and 1920 on account of the good will of the wholesale liquor business of Schuetz, Renziehausen & Company, a partnership in which he owned a one-half interest; this deduction to be based on a March 1, 1913, value of $115,000.

Respondent's position is that the Board of Tax Appeals and the Circuit Court of Appeals correctly held that the deductions were not allowable since it was not the legislative intent in enacting Section 214 (a) (8) of the Revenue Acts of 1918 and 1921 to provide an obsolescence deduction for intangibles

such as good will, trade-marks, trade brands or trade names.

The argument in support of this position is substantially identical with that made in the brief for the collector in *Clarke, Collector,* v. *The Haberle Crystal Springs Brewing Company,* No. 68, October Term, 1929, copies of which we have supplied to counsel for the petitioner herein. The discussion in the *Clarke case* was limited to obsolescence of good will under Section 234 (a)(7) of the Revenue Act of 1918, the provisions of which are identical with those of Section 214 (a) (8) of the Revenue Acts of 1918 and 1921. The value of the trade-marks, trade brands, and trade names is so dependent upon and so closely related to good will that all may properly be considered as a single class. Petitioner has not undertaken to segregate them. The argument for the Collector in the *Clarke case* regarding obsolescence of good will is equally applicable to the good will, trade-marks, trade brands, and trade names in the instant case.

It is submitted further that, even if it were to be admitted that an obsolescence deduction may be applied to good will, under the facts in this record, which differ from those in the *Clarke case, supra,* in the respects mentioned below, no such deduction may be allowed for the intangibles of the distilling business during the years 1918, 1919, 1920, and 1921. The *Clarke case* involved the good will of a brewery, the product of which was not required for

medicinal purposes after the enactment of prohibition legislation, as was the petitioner's distillery product. Also, in that case it was found as a fact that national prohibition destroyed the good will of the Haberle Crystal Springs Brewing Company. There is no such finding here. As long as the petitioner herein was able to manufacture or dispose of his product, the good will of his business was not obsolete, and until obsoleteness may reasonably be foreseen there is no obsolescence in fact. For the reasons set forth herein under point III in the discussion of the disallowance of obsolescence deductions for the tangible assets, we contend that the evidence in this case shows clearly that there was no obsolescence in fact of the good will during the taxable years. Therefore, to avoid repetition, we respectfully refer the Court to our argument under point III.

II

THE PETITIONER IS NOT ENTITLED TO A DEDUCTION IN 1919 FOR LOSS OF THE INTANGIBLE PROPERTIES OF THE DISTILLING BUSINESS UNDER SECTION 214 (A) (4) OF THE REVENUE ACT OF 1918

The petitioner contends in the alternative that if deductions for obsolescence of the good will, trademarks, trade brands and trade names of the distilling business are not allowable for the years 1918 to 1921, inclusive, he is entitled under Section 214 (a) (4) of the Revenue Act of 1918 to a deduction in 1919 for the loss of such properties based on their cost.

This section only permits the deduction of losses "sustained during the taxable year," and refers to losses actually realized. *Brewer* v. *Orr,* 19 F. (2d) 230. The provision necessarily requires that it be a complete and definitely ascertained loss fixed by an identified event such as an actual abandonment, a sale or a destruction of the property. Cf. *United States* v. *White Dental Co.,* 274 U. S. 398, 401; *Lewellyn* v. *Elec. Reduction Co.,* 275 U. S. 243, 246–247; Regulations 45 (1920 Ed.), Arts. 141, 143.

Good will is only an incident to a going concern or business having locality or name, and is not susceptible of being disposed of independently. *Metropolitan Bank* v. *St. Louis Dispatch Co.,* 149 U. S. 436, 446. The petitioner's good will and the value of the trade-marks, trade brands, and trade names were inseparable from the business itself and a loss on account of such intangibles can therefore only be reflected in the loss sustained in the sale or abandonment of the business. In denying a claim similar to that made by the petitioner, the Circuit Court of Appeals for the Eighth Circuit in *Red Wing Malting Co.* v. *Willcuts,* 15 F. (2d) 626, certiorari denied, 273 U. S. 763, said in part (pp. 633–634):

> We turn, therefore, to the question of whether the allowance claimed can be made under section 234 (a), subsection (4). It is suggested in the reply brief of plaintiff that, if defendant's argument be conceded to be correct as to the obsolescence feature

of the statute, this court could decide the case under the loss section, section 234 (a), subsection (4)[1] hereinbefore set out, and it is claimed that under the pleadings the requested allowance could be granted under that subsection as a loss sustained in plaintiff's fiscal year ending August 31, 1918.

* * * * *

We have heretofore pointed out that good will has no existence separate and apart from an established business. With the termination of that business it is ended. While a capital asset, it is not the subject of purchase, sale, or assignment separate from the business itself. It is not an assignable asset distinct from the business. It is different in this respect from such intangibles as patents, contracts or franchises which may be sold. When a business is disposed of its value and realized selling price may be enhanced by the existence of good will. If sold at a loss, the loss of good will is reflected in the transaction. The claim is somewhat novel, therefore, and rather startling, that loss of good will can be made the subject of an independent claim for a tax reduction, separate and distinct from the business of which it is an incident.

When the property of the Red Wing Malting Company was sold at a depreciated value by reason of prohibition, the loss of good will was reflected in the general loss. This loss might possibly be a basis for a deduction un-

[1] The section referred to applies to corporations as does Section 214 (a) (4) to individuals and is in the same words.

> der section 234 (a), subsection (4), of the statute. We are not advised whether or not such allowance has been made. To hold that a claimant is entitled to segregate good will from the property and business to which it is attached as an incident, and from which it is inseparable, and permit a separate deduction for its loss, might result in a double deduction and have far-reaching consequences. If the court is to open the door to claimants for tax deductions under the statute for the loss of good will apart from the tangible property with which it is connected, the right should clearly appear from the statute. We think it does not so appear.

It is submitted that the findings show that a loss of good will, trade-marks, trade brands, or trade names was not sustained in the year 1919. During that year and succeeding years until the late fall of 1921, the petitioner continued to manufacture whiskey and to sell his product to persons or firms having Government permits to buy for medicinal purposes. As late as 1921 the petitioner expended money for advertising. (R. 33.) After the enactment of the Willis-Campbell Act distilling operations ceased, but the petitioner continued to dispose of the whiskey on hand. The good will, trade-marks, trade brands, and trade names were not abandoned, discarded, or lost during the year 1919. Under these facts, a deductible loss was not sustained. Cf. *Dick & Brothers Quincy Brewing Co.* v. *United States,* No. F–146, United States

Court of Claims, decided May 6, 1929. These intangibles may have suffered a substantial decline in value, but "the statute obviously does not contemplate and the regulations (Art. 144) forbid the deduction of losses resulting from the mere fluctuation in value of property owned by the taxpayer." *United States* v. *White Dental Co., supra,* p. 401.

Moreover, the principle announced in the *Red Wing case* is correct, and since there was no sale or abandonment of the petitioner's business during the year 1919 there could not be a separate and independent deduction in the year for loss of good will.

Even if the loss deduction could otherwise be allowed for the year 1919, there is no adequate proof of the cost of the intangible assets and therefore nothing upon which the amount of the loss, if any, can be determined. The cost is alleged to have been incurred as follows (R. 40):

For services rendered by petitioner without compensation 1884 to 1913 (29 years at $15,000 per annum)	$435,000.00
Advertising, 1899 to 1913	82,500.02
Leakage, 1899 to 1913	55,781.10
Trade-mark acquired for cash, July 19, 1897	5,000.00
Total cost of intangibles	578,281.12

It is difficult to follow the contention of the petitioner that the total value of his services for twenty-nine years at $15,000 a year was part of the cost of any of the intangible assets. After the year 1897 he operated the Large Distillery as a sole proprietorship. In other words, the Large Distilling Company was Frederick C. Renziehausen. It made no

difference whether he paid himself a salary of $15,000 a year or withdrew that amount as profits. But assuming that the Large Distilling Company may be considered as an entity separate from the petitioner, the fact that it paid him no salary meant only that the cost of the liquor produced each year was just that much less and the profits—his profits—just that much more. But in no event could the value of his services be a part of the cost of good will.

Neither can it be said without further proof that the cost of advertising was part of the cost of the intangible assets. Advertising is one of the most ordinary and necessary expenses for each year's business. Only under unusual circumstances do expenditures for advertising comprise a part of the cost of good will. Cf. Article 101, Regulations 45; *Richmond Hosiery Mills* v. *Commissioner,* 29 F. (2d) 262, certiorari denied, 279 U. S. 844.

The petitioner also contends that the amounts paid for leakage constituted part of the cost of the intangible assets. The purpose in making the payments does not appear. If they were ordinary and necessary expenses, as they seem to have been, they were no part of the cost of the intangible assets.

All of the amounts which it is contended constituted the cost of the good will, with the exception of the amount of $5,000 cash paid out for a trade mark in 1897, are in the usual course ordinary and necessary business expenses. Salaries and adver-

tising are paid for every year. They enter into the cost of the year's output and do not normally go into the purchase price of any capital asset. The same is true of the amounts paid for leakage. If any part of the amounts paid for the various items do constitute capital expenditures, there is nothing in the record to show how much went into the purchase of the intangible assets and how much constituted the ordinary business expenses. The petitioner had the burden of proving his right to the deduction and the amount to which he was entitled. It is significant that the Board, although requested by the petitioner so to do, failed to find the cost of the good will. From the evidence adduced it was impossible.

It is submitted that the petitioner is not entitled to a deduction for obsoleteness of the intangible assets and that in any event there is no proof of the cost of the assets upon which to base a loss deduction.

III

THE PETITIONER IS NOT ENTITLED TO DEDUCTIONS FROM INCOME FOR THE YEARS 1918 TO 1921, INCLUSIVE, OF ANY AMOUNTS FOR THE OBSOLESCENCE OF THE TANGIBLE PROPERTY OF THE LARGE DISTILLING COMPANY IN EXCESS OF THE DEDUCTIONS ALLOWED BY THE BOARD OF TAX APPEALS

The petitioner claims the right to a deduction for obsolescence of his plant, equipment, and warehouses for the years 1918 to 1921, inclusive, under Section 214 (a) (8) of the Revenue Acts of 1918

and 1921. It will be noted that the Board of Tax Appeals allowed a deduction for 1921 of the depreciated cost of the plant and equipment less the salvage value, exclusive of warehouses, or $147,582.06. (R. 43.) This was permitted on the theory that it was a loss sustained for obsoleteness of such property caused by the enactment on November 23, 1921, of the Willis-Campbell Act, prohibiting the manufacture of spirituous liquor for medicinal purposes except under permit from the Commissioner, as a result of which the petitioner abandoned distilling operations and ceased to use the plant and equipment. The Board also held that as a result of the Willis-Campbell Act obsolescence of the warehouses began in 1921 and consequently allowed for 1921 and 1922 a deduction for obsolescence based upon the proportionate loss of usefulness of the warehouses. (R. 43–45.) These allowances were affirmed by the Circuit Court of Appeals. (R. 116–117.) Deductions for obsolescence of the tangible properties were disallowed for 1918, 1919, and 1920.

Obsolescence is the state of becoming obsolete. Obsoleteness refers to a situation where the commercial usefulness of an asset ends before the expiration of its physical life. The state of obsoleteness is reached when property which can not be used for any other purpose is no longer useful for the purpose for which it was acquired. From its very nature, therefore, obsolescence begins only when, from the existing facts, a taxpayer has sub-

stantial reason to believe that assets would not be useful in his own or any other business at some fairly definite time in the future when they must be abandoned before the expiration of their normal physical life. *Cf. Lassen Lumber & Box Co.* v. *Blair,* 27 F. (2d) 17. It is submitted, therefore, that the material and controlling fact necessary to sustain such deductions in the years 1918, 1919, or 1920, must be present, namely, that it must have been known with reasonable certainty that the commercial usefulness of the petitioner's plant and equipment would end at a fairly definite time before the expiration of their physical life. This controlling fact is lacking in the instant case and the evidence supports the view that in those years these assets were not obsolescing.

The petitioner testified that in 1918 he believed the whiskey business was through, that "the jig was up." However, in 1919 he had occasion to revise his opinion when he saw that he would still be able to manufacture and dispose of his product for medicinal uses. (R. 77.) This manufacture was continued until in November, 1921, the enactment of the Willis-Campbell Act and the refusal of the Commissioner to issue permits caused the petitioner to discontinue his distilling operations. The enactment of that Act and the Commissioner's refusal were the events which caused his plant and equipment to be abandoned. The petitioner manufactured 396 barrels of medicinal whiskey in 1919, 5,858 barrels in 1920, and 10,400 barrels in 1921 up

to November 23. Had it not been for the enactment of the Willis-Campbell Act in 1921, the plant and equipment would not have become obsolete in that year.

From the petitioner's testimony it appears that this legislation was not foreseen during the years 1918, 1919, and 1920 or at any time prior to its enactment. He testified (R. 77–78):

> In the fall or summer of 1919, we found out that we were mistaken in the assumption in 1918 that the business would have to be wound up in four years, and we kept on making whiskey until the passage of the Willis-Campbell Act. The brewers wanted to make whiskey and Senator Willis wanted to stop them and he commenced to jamb what was known as a beer bill through Congress and they put in that joker that distilleries would have to stop manufacturing whiskey, too, and we made whiskey up until the 23d. If the old brewers had stayed out we would be making whiskey today.
>
> Q. It was a bolt out of a clear sky, wasn't it?
>
> A. What is that?
>
> Q. That was a bolt out of a clear sky?
>
> A. We did not know.
>
> We did not think that the Republican Party would allow the Willis-Campbell Act to pass. The whole thing was in the Democratic Party, and the Republicans ought to have kept their hands off. They ought to have pulled Willis away and say "lay low."

In view of this testimony, the argument in petitioner's brief (p. 35) that the Willis-Campbell Act was foreseen loses its force. As the petitioner was enabled to continue and did continue the use of his plant and equipment and warehouses during the taxable years, and as there were no reasonable grounds to believe at that time that the use would be destroyed, there was no obsolescence in fact and no deduction should be allowed.

Further, in order to allow deductions for obsolescence there must be some basis upon which the amount can be computed. In the case of ordinary depreciation it is known with reasonable certainty what the life of the property will be and consequently depreciation can be computed upon that basis. In such cases there is always a time when the depreciation commences and a time when it ends. In the case of obsolescence, which is only accelerated depreciation, it is likewise necessary to know approximately when the obsolescence commences and when it ends. The petitioner apparently contends that the obsolescense of his tangible properties commenced with the submission by Congress of the Eighteenth Amendment to the various States and that the obsolescence ended with the passage of the Willis-Campbell Act.

The submission by Congress of the Eighteenth Amendment to the various States did not start obsolescence of the petitioner's tangible properties. As heretofore shown, he continued to use those

tangible properties until 1921. Likewise, in 1918 it could not have been said that the Willis-Campbell Act would be passed in 1921, nor did that Act, when finally passed, end any period of obsolescence. In other words, there is no basis upon which obsolescence deductions could be based. There is no point of time at which it could be said that obsolescence started nor is there any point of time at which it can be said that obsolescence was complete. The loss of usefulness or the obsoleteness of the petitioner's plant and equipment was not foreseen nor was it gradual; it was sudden and complete. This loss has been allowed by the Board for 1921, and the allowance has been sustained by the Circuit Court of Appeals. The gradual loss of useful value of the warehouses began in 1921 and likewise has been allowed.

In this proceeding before the Board, the petitioner bore the burden of proof. Cf. *United States* v. *Rindskopf*, 105 U. S. 418; *Wickwire* v. *Reinecke*, 275 U. S. 101; *Botany Mills* v. *United States*, 278 U. S. 282. To justify a deduction for obsolescence it was incumbent on him to show the cardinal fact that obsoleteness at some fairly definite time in the future could be anticipated.

We submit that this fact was not proved and that on the contrary the evidence shows that obsoleteness was not foreseen. In the absence of this controlling fact, the disallowance of the deductions should be sustained. *Botany Mills* v. *United States, supra.*

IV

THE PETITIONER IS NOT ENTITLED TO HAVE THE PROFIT FROM THE SALE OF WHISKEY IN 1922 TAXED AS A CAPITAL GAIN, UNDER SECTION 206 OF THE REVENUE ACT OF 1921

The petitioner contends that the sale of the "old whiskey" in 1922 was a sale of capital assets within the meaning of Section 206 (a) (6) of the Revenue Act of 1921 and taxable at the rate of 12½% in accordance with the provisions of Section 206 instead of at the usual normal and surtax rates. Section 206 (a) (6) provides that the term "capital assets" as used in the section means property acquired and held by the taxpayer for profit or investment for more than two years, not including stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year.

The petitioner and the Large Distilling Company were one and the same; the Large Distilling Company was simply the name under which the petitioner as an individual traded and did business. (R. 79.) Such business embraced both the manufacture of whiskey and its sale and the "old whiskey" account carried on the books merely represented whiskey manufactured but not sold during the year in which it was manufactured. Portions of such whiskey were sold at various stages of maturity in years prior to 1922, the year here involved. (R. 31.)

The petitioner attempts to make a distinction between the manufacture of whiskey on contract and

the manufacture of whiskey not on contract and the aging and holding of it for future sale. The distinction, if any, is one without a difference. In both cases the whiskey manufactured, whether represented by warehouse receipts or contracts or by the actual whiskey itself, was the stock in trade and inventory of the manufacturer. The taxpayer in this case was engaged in both businesses. He manufactured whiskey previously sold on contract. He also manufactured whiskey, kept it and aged it, and later sold it. Whiskey of the latter class was in no sense a capital asset within the general meaning of the term, which contemplates a permanent business asset the use or employment of which gives rise to income. It was not *acquired* for investment within the meaning of the Act, since it merely represented whiskey manufactured for sale in the usual course of petitioner's business and remaining unsold at the end of the year.

It may be noted that in the petitioner's statement of the case (Br., p. 6) it is said that in 1908 he commenced to invest his excess funds in this whiskey. The only finding in this respect is as follows (R. 39):

> In 1908 there was opened on the books of the Large Distilling Company an account captioned "Old Whiskey." At the close of each distilling season the whiskey manufactured and not sold was charged to this account and carried to maturity when it was sold to the trade through the organization of the Large Distilling Company. * * *

> Renziehausen regarded the whiskey carried in this account as a personal investment. Over a long period of time the petitioner Renziehausen had carried personal investments on the books of the Large Distilling Company.

This is entirely consistent with the respondent's position that the whiskey represented the product of the petitioner, manufactured and sold in the usual course of his business. We submit that the whiskey, whether old or new, represented income arising from the employment of capital assets and labor and not an asset acquired for profit or investment within the meaning of Section 206 (a) (6).

The old whiskey was stock in trade, to be included in the petitioner's inventory if on hand at the end of the year with as much reason as unsold whiskey manufactured during the year. Time was required to age it and the aging was only a part of the normal process of its manufacture. The treatment in a separate account or the fact that the old whiskey remained on hand for more than two years before sale can not change its character from stock in trade to a capital asset. We submit that no essential difference exists between the old whiskey and any goods purchased by a merchant or manufactured in a business and not sold within two years from the time of such purchase or manufacture.

The petitioner contends that as the business of the Large Distilling Company was in the process

of liquidation after November 23, 1921, all stock in trade or inventory became a capital asset. The evidence does not show the nature of the liquidation or what steps had been taken in 1921 or 1922. No reason is shown or can be perceived to indicate that the beginning of liquidation could change the character of inventoriable stock in trade and work a conversion into capital assets. And, as has been pointed out, the Act requires that the asset shall be *acquired* for profit or investment; and if it is not originally so acquired, but was acquired by manufacture for sale in the usual course of the petitioner's business, liquidation can not relate back to or alter the purpose of the acquisition.

It is submitted that the profits realized on the sale in 1922 of whiskey carried in the "old whiskey" account can not be taxed specially under the capital gain provisions of Section 206 of the Revenue Act of 1921.

CONCLUSION

It is respectfully submitted that the judgment of the Circuit Court of Appeals should be affirmed.

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JANUARY, 1930.

U. S. GOVERNMENT PRINTING OFFICE: 1930

SUPREME COURT OF THE UNITED STATES.

No. 114.—October Term, 1929.

Frederick C. Renziehausen, Petitioner, *vs.* Robert H. Lucas, Commissioner of Internal Revenue.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

[January 27, 1930.]

Mr. Justice Holmes delivered the opinion of the Court.

This case raises the same questions as the preceding one, *Clarke* v. *Haberle Crystal Springs Brewing Co.*, but was decided the other way. 31 F. (2d) 675. A writ of certiorari was granted by this Court on October 14, 1929.

The good will here concerned, (treated as embracing trade-marks, trade brands and trade names,) was that of a business of distilling and selling whiskey, warehousing, and a wholesale liquor business. The Board of Tax Appeals adjudged a deficiency in the petitioner's income tax returns for 1918, 1919, 1920 and 1922. A deduction is claimed by him, as in the other case, for exhaustion or obsolescence of the good will, under the Revenue Act of 1918, (Act of February 24, 1919,) c. 18, § 214 (a) (8); 40 Stat. 1057, 1067, using the same words for individuals that are used in § 234 for corporations, and under the Revenue Act of 1921, (Act of November 23, 1921,) c. 136, § 214 (a) (8); 42 Stat. 227, 240, using the same words again. What has been said in the *Haberle Crystal Springs Brewing Co.'s* case is sufficient to dispose of this one, and here there is the additional fact that in 1919 the petitioner became aware that he could manufacture whiskey for medicinal purposes and did so until the Willis-Campbell Act of November 23, 1921, c. 134; 42 Stat. 222, was passed and the petitioner failed to obtain a permit under it. The evidence does not seem to warrant an alternative claim under the Revenue Act of 1918, § 214 (a) (4), for losses incurred in business in 1919, even if otherwise it could be sustained.

The only other question that seems to need mention is raised by an account headed "Old Whiskey", on the books of the Large

Distilling Company, under which name the petitioner did the distilling business. At the close of each distilling season the whiskey manufactured and not sold was charged to this account, matured and sold to the trade. The petitioner regarded this whiskey as a personal investment, but the whole business was his, and we agree with the Circuit Court of Appeals that the whiskey was clearly a part of the stock in trade, and therefore that he was not entitled to the more favorable rate allowed by the Act of November 23, 1921, c. 136, § 206 (6), for taxes on capital gain, excluding stock in trade. The petitioner has no reason to complain of the allowance for obsolescence of the warehouses.

Decree affirmed.

Mr. Justice McREYNOLDS and Mr. Justice STONE concur in the result.